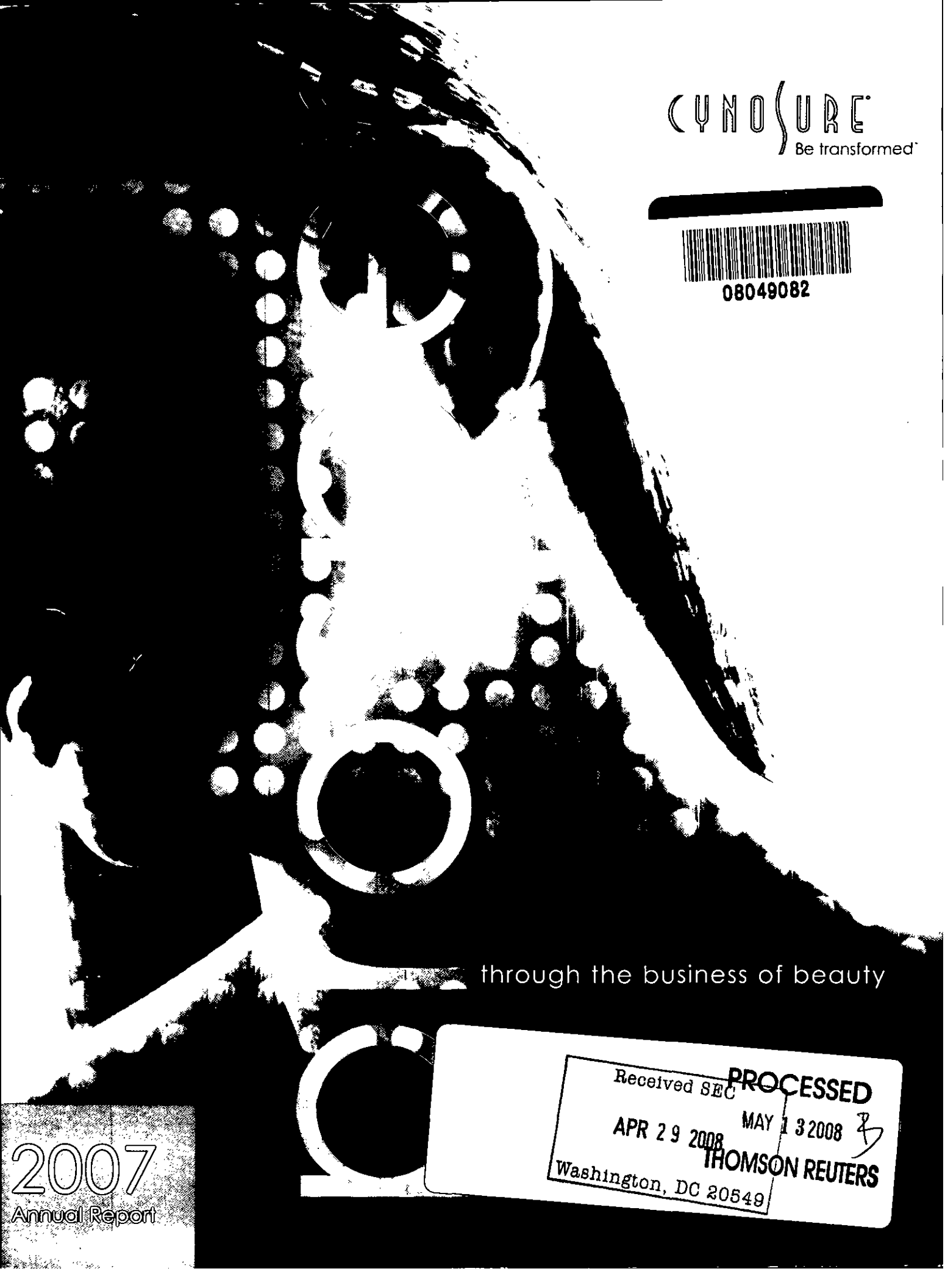


Dear Shareholders,

Powered by momentum across our entire line of flagship products, Cynosure delivered record financial results in 2007, posting net income of $14.5 million and increasing revenue by 59% to $124.3 million. This outstanding performance reflects a unique strength of our company — the ability to combine innovative technology, differentiated products and strong distribution to rapidly build a leadership position in the fastest-growing segments of the aesthetic market.

New Products

Smartlipo™, our new aesthetic laser for body sculpting, and Affirm™, our versatile workstation for anti-aging applications, exemplify our success in high-growth markets. Channeled through our expanding direct distribution sales organization, Affirm and Smartlipo helped to increase our gross margin in 2007 to 64% from 58% in 2006. In addition, these new applications expand upon our strong base business in more traditional areas such as hair removal and the treatment of vascular and pigmented lesions.

The strength and pace of our product development can be summarized in a single sentence: In 2007, 100% of our laser product revenue came from products we have introduced since 2004. Behind our performance is a commitment to manufacture and service highly differentiated, upgradeable products that encompass the spectrum of cosmetic energy sources. By combining multiple energy sources in a single system, Cynosure's products enable physicians, aestheticians and spas to capitalize efficiently on the accelerating consumer demand for a variety of cosmetic procedures.

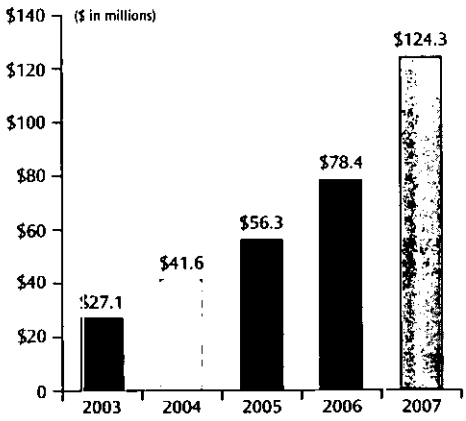
One example of our commitment was our introduction of a new 1320 nm wavelength Nd:YAG laser for our flagship Affirm workstation for tissue tightening as a result of tissue coagulation. This additional laser complemented the 1440 nm Nd:YAG laser for skin micro-rejuvenation and the Xenon Pulsed Light system for skin discoloration. The Affirm is the only anti-aging system to couple Cynosure's proprietary Combined Apex Pulse™ (CAP) and MultiPlex™ technology in one device. The CAP technology is a distinctive, high-density disposable lens array that redistributes laser energy in a combination of high and low level heat to stimulate and remodel collagen production throughout the treatment area. The system utilizes Cynosure's patented MultiPlex technology to enable the rapid sequential emission of two wavelengths, 1320 nm and 1440 nm, from the same optical fiber with a short delay between fixed pulses.

We also recently introduced the Affirm Er 2940 nm Erbium YAG laser for Affirm. The Affirm Er handpiece broadens the capabilities of the existing platform with the addition of ablative skin resurfacing, a growing area of interest among consumers who want to reduce deep lines and wrinkles. Millennium Research Group projects that the anti-aging, skin rejuvenation market is growing at 18% annually and by 2010 will be valued at $239 million.

Laser lipolysis also is a major growth engine for Cynosure. Of the nearly 12 million cosmetic procedures performed in the United States in 2007, approximately 500,000 involved liposuction, the leading surgical cosmetic application for men and women. Liposuction is a complex surgical procedure that involves the removal of fat from the body, often resulting in significant bleeding and bruising as well as an extended period of recovery. Smartlipo, by contrast, provides aesthetic surgeons with a minimally invasive tool to target and remove small, localized areas of unwanted fat. Because Smartlipo typically requires less downtime and causes minimal trauma to the treated area, the technology is proving to be an exciting option for physicians and patients.

Smartlipo is a proprietary technology that uses a 1064 nm Nd:YAG laser fiber, channeled through a small cannula, to rupture and liquefy subcutaneous fat cells and tighten the surrounding tissue. We estimate that aesthetic surgeons have performed several thousand Smartlipo procedures since the product was launched. We expect that figure to increase significantly with our recent introduction, at the 2007 American Society of Plastic Surgeons meeting, of an 18-watt Smartlipo. With this new higher-powered system, an area of localized abdominal fat can be treated in about 12 minutes versus 35 minutes with the original 6-watt Smartlipo system we initially introduced in 2006.

Five-year Compound Annual Revenue Growth of 36%



Recently we introduced SmartSense™, a proprietary intelligent delivery system for Smartlipo. SmartSense features an advanced microchip that delivers the precise level of energy based on the area of treatment and the motion of the handpiece. Because SmartSense prevents the laser from firing when the handpiece motion stops, the technology offers greater control for the aesthetic surgeon and an additional layer of safety for the patient.

Accolade™, Cynosure's sixth and newest flagship product, is our new 755 nm Q-switched Alexandrite laser for the removal of benign cutaneous pigmented lesions as well as certain multi-colored tattoos. Because of the prevalence of pigmented lesions among Asian populations, Japan, Korea and China will be among our initial target markets, followed by Europe and Latin America. Given the size of the pigmented lesion market, we are excited about the long-term prospects for Accolade, particularly as we continue to build our international sales force.

North American Direct Sales Force Expansion

In 2007, we expanded our North American direct sales force by more than 40% to 66 representatives, which included 15 surgical specialty sales reps marketing Smartlipo in the United States and Canada. We reinforced their efforts by establishing product training centers and hosting a variety of special events including forums, workshops and webinars. Our focus on building our direct sales force yielded positive results in 2007, as the percentage of revenue from products sold in North America increased 85% to $73.7 million from $39.8 million in 2006.

International Markets

At the end of 2007, our international distribution was comprised of 27 direct sales reps in six countries and 19 distributors covering 44 countries. In 2007, 33% of our laser product revenue originated outside of North America. We continue to establish key distribution relationships for Cynosure in the Middle East and northern Europe and are also building marketing momentum in Asia. In late 2006, we became the first U.S. aesthetic laser company to establish a wholly owned subsidiary in China, and in June 2007 we received regulatory approval in China to market and sell our Elite™ family of laser workstations that permanently remove hair and treat benign epidermal pigmented lesions. To extend our position in this rapidly emerging cosmetic marketplace, we plan to open additional offices in the Asia-Pacific region in 2008.

Positioned for Growth

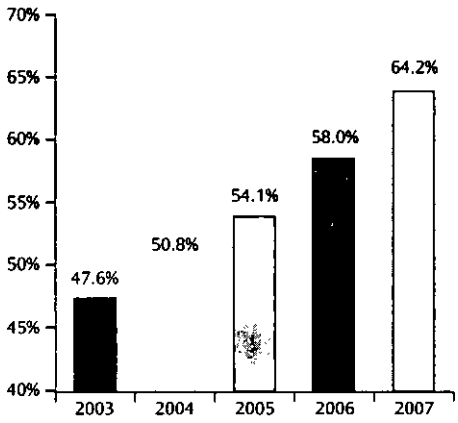
Following an outstanding year in 2007, we expect to maintain a strong growth trajectory in the year ahead. The Cynosure brand has become synonymous with expanding the market through technology innovation while continuing to work closely with customers to build their practices. We believe new products and additional distribution expansion will continue to feature prominently in our plans for 2008, which include the projected international launch of Smartlipo, as well as continued sales force expansion in the U.S. and abroad.

Today, cosmetic procedures are more affordable and accessible than ever before. The trends are favorable for both the applications and providers we are targeting. We have the entrepreneurial passion, product excellence and management skill to extend our leadership in the aesthetic industry. On behalf of our employees and board of directors, I thank our customers, partners and you, our shareholders, for your confidence and trust in Cynosure.

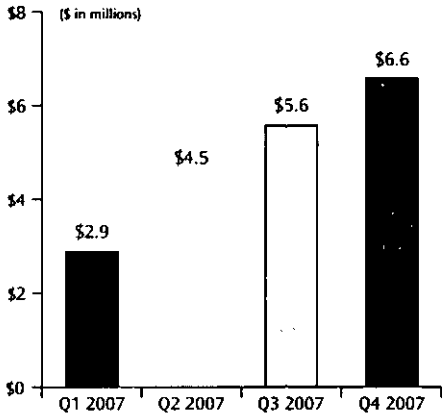
Sincerely,

Michael Davin
Chairman, President and Chief Executive Officer
March 27, 2008

New Products, Effective Distribution Fuel Gross Margin Expansion



Steadily Increasing Operating Income in 2007



UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-K

(Mark One)

☒ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2007

OR

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from to

Commission file number 000-51623

Cynosure, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**04-3125110**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
5 Carlisle Road Westford, MA	**01886**
(Address of principal executive offices)	**(Zip Code)**

Registrant's telephone number, including area code
(978) 256-4200

Securities registered pursuant to Section 12(b) of the Act:
Class A Common Stock, $0.001 par value

Securities registered pursuant to Section 12(g) of the Act:
None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☐ No ☒

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ☐ No ☒

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☒

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ☐ Accelerated filer ☒ Non-accelerated filer ☐ Smaller reporting company ☐
(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes☐ No ☒

Aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant, based on the last sale price for such stock on June 29, 2007: $304,393,524.

The number of shares outstanding of each of the registrant's classes of common stock, as of March 7, 2008:

Class	Number of Shares
Class A Common Stock, $0.001 par value	9,541,184
Class B Common Stock, $0.001 par value	2,975,297

Portions of the registrant's definitive Proxy Statement for its 2008 Annual Meeting of Stockholders are incorporated by reference into Part III of this Annual Report.

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FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K contains forward-looking statements that involve substantial risks and uncertainties. All statements, other than statements of historical facts, included in this Annual Report regarding our strategy, future operations, future financial position, future revenues, projected costs, prospects, plans, objectives of management and expected market growth are forward-looking statements. The words "anticipate," "believe," "estimate," "expect," "intend," "may," "plan," "predict," "project," "will," "would" and similar expressions are intended to identify forward-looking statements, although not all forward-looking statements contain these identifying words. These forward-looking statements include, among other things, statements about:

- our ability to identify and penetrate new markets for our products and technology;
- our ability to innovate, develop and commercialize new products;
- our ability to obtain and maintain regulatory clearances;
- our sales and marketing capabilities and strategy in the United States and internationally;
- our intellectual property portfolio; and
- our estimates regarding expenses, future revenues, capital requirements and needs for additional financing.

We may not actually achieve the plans, intentions or expectations disclosed in our forward-looking statements, and you should not place undue reliance on our forward-looking statements. Actual results or events could differ materially from the plans, intentions and expectations disclosed in the forward-looking statements we make. We have included important factors in the cautionary statements included in this Annual Report, particularly in Item 1A of this Annual Report, and in our other public filings with the Securities and Exchange Commission that could cause actual results or events to differ materially from the forward-looking statements that we make.

You should read this Annual Report and the documents that we have filed as exhibits to the Annual Report completely and with the understanding that our actual future results may be materially different from what we expect. It is routine for internal projections and expectations to change as the year or each quarter in the year progresses, and therefore it should be clearly understood that the internal projections and beliefs upon which we base our expectations are made as of the date of this Annual Report and may change prior to the end of each quarter or the year. While we may elect to update forward-looking statements at some point in the future, we do not undertake any obligation to update any forward-looking statements whether as a result of new information, future events or otherwise, except as required by law.

PART I

Item 1. *Business*

Overview

We develop and market aesthetic treatment systems that are used by physicians and other practitioners to perform non-invasive procedures to remove hair, treat vascular lesions, rejuvenate skin through the treatment of shallow vascular lesions and pigmented lesions, temporarily reduce the appearance of cellulite, treat wrinkles, skin texture, skin discoloration and skin tightening, and to perform minimally invasive procedures for LaserBodySculpting for the removal of unwanted fat. Our systems incorporate a broad range of laser and other light-based energy sources, including Alexandrite, pulse dye, Nd:Yag and diode lasers, as well as intense pulsed light. We believe that we are one of only a few companies that currently offer aesthetic treatment systems utilizing Alexandrite and pulse dye lasers, which are particularly well suited for some applications and skin types. We offer single energy source systems as well as workstations that incorporate two or more different types of lasers or pulsed light technologies. We offer multiple technologies and system alternatives at a variety of price points depending primarily on the number and type of energy sources included in the system. Our newer products are designed to be easily upgradeable to add additional energy sources and handpieces, which provides our customers with technological flexibility as they expand their practices. As the aesthetic treatment market evolves to include new customers, such as aesthetic spas and additional physician specialties, we believe that our broad technology base and tailored solutions will provide us with a competitive advantage.

We sell 16 different aesthetic treatment systems and have focused our development and marketing efforts on offering leading, or flagship, products for each of the major aesthetic procedure categories that we address. Our flagship products are:

- the *Apogee Elite* system for hair removal;
- the *Cynergy* system for the treatment of vascular lesions;
- the *TriActive LaserDermology* system for the temporary reduction of the appearance of cellulite;
- the *Affirm* system for anti-aging, including treatments for wrinkles, skin texture, skin discoloration and skin tightening; and
- the *Smartlipo* system for LaserBodySculpting℠ for the removal of unwanted fat.

In addition to their primary applications, the *Apogee Elite* and *Cynergy* systems can each be used by practitioners for a variety of other applications.

In January 2008, we introduced the *Accolade*, our sixth flagship product, which is a high powered 755nm, Q-switched Alexandrite laser for the removal of benign pigmented lesions, including pigmented lesions known as Nevus of Ota and Nevus of Ito, as well as multi-colored tattoos.

We sell our products through a direct sales force in North America, four European countries, Japan and China and through international distributors in 44 other countries. As of December 31, 2007, we had sold more than 7,100 aesthetic treatment systems worldwide. See Note 6 to our Consolidated Financial Statements for revenue, net asset and long-lived asset information by geographic region.

Corporate Information

We were incorporated under the laws of the State of Delaware in July 1991. Our principal executive offices are located at 5 Carlisle Road, Westford, Massachusetts 01886, and our telephone number is (978) 256-4200.

We are subject to the informational requirements of the Securities Exchange Act of 1934, as amended, and, accordingly, file reports, proxy statements and other information with the Securities and Exchange Commission.

Such reports, proxy statements and other information can be read and copied at the public reference facilities maintained by the Securities and Exchange Commission at the Public Reference Room, 100 F Street, NE, Room 1580, Washington, D.C. 20549. Information regarding the operation of the Public Reference Room may be obtained by calling the Securities and Exchange Commission at 1-800-SEC-0330. The Securities and Exchange Commission maintains a website (http://www.sec.gov) that contains material regarding issuers that file electronically with the Securities and Exchange Commission.

Our website address is www.cynosure.com. The information on our website is not a part of this Annual Report. We make available free of charge on our website our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, as soon as reasonably practicable after we electronically file such material with, or furnish it to, the Securities and Exchange Commission.

Industry

Aesthetic Market Opportunity

Michael Moretti/Medical Insight, Inc., an independent aesthetic treatment market research firm, estimates that the number of non-invasive aesthetic treatment procedures worldwide using laser and other light-based technologies will grow from nearly 58 million in 2006 to over 170 million in 2011, representing a compound annual growth rate of over 24%. We estimate that the worldwide market for aesthetic treatment systems based on laser and other light-based technologies exceeded $1 billion in 2007. We base this estimate on published market research reports, revenue figures for public companies and our conversations with the managements of private companies that compete in the aesthetic treatment equipment market.

Key factors contributing to growth in the markets for aesthetic treatment procedures and aesthetic laser equipment include:

- the aging population of industrialized countries and the rising discretionary income of the "baby boomer" demographic segment;
- the desire of many individuals to improve their appearance;
- the development of technology that allows for safe and effective aesthetic treatment procedures;
- the impact of managed care and reimbursement on physician economics, which has motivated physicians to establish or expand their elective aesthetic practices with procedures that are paid for directly by patients; and
- reductions in cost per procedure, which has attracted a broader base of clients and patients for aesthetic treatment procedures.

Expansion Into Non-Traditional Physician Customer and Medi-Spa Markets

Aesthetic treatment procedures that use lasers and other light-based equipment have traditionally been performed by dermatologists and plastic surgeons. Based on published membership information from professional medical organizations, there are approximately 18,000 dermatologists and plastic surgeons in the United States. More recently, a broader group of physicians in the United States, including primary care physicians, obstetricians, gynecologists, ophthalmologists and ear, nose and throat specialists, have incorporated aesthetic treatment procedures into their practices. These non-traditional physician customers are largely motivated to offer aesthetic procedures by the potential for a reliable revenue stream that is unaffected by managed care and government payor reimbursement economics. We believe that there are approximately 200,000 of these potential non-traditional physician customers in the United States and Canada, representing a significant market opportunity that is only beginning to be addressed by suppliers of lasers and other light-based aesthetic equipment. Some physicians are electing to open medical spas, often adjacent to their conventional office space, where they perform aesthetic procedures in an environment designed to feel less like a health care facility.

The Structure of Skin and Conditions that Affect Appearance

The human skin consists of several layers. The epidermis is the outer layer and contains the cells that determine pigmentation, or skin color. The dermis is a thicker inner layer that contains hair follicles and large and small blood vessels. Beneath the dermis is a layer that contains subdermal fat and collagen, which provides strength and flexibility to the skin.

The appearance of the skin may change over time due to a variety of factors, including age, sun damage, circulatory changes, deterioration of collagen and the human body's diminished ability to repair and renew itself. These changes include:

- unwanted hair growth;
- uneven pigmentation;
- wrinkles;
- blood vessels and veins that are visible at the skin's surface; and
- the appearance of cellulite.

Changes to the skin caused by pigmentation are called pigmented lesions and are the result of the accumulation of excess melanin, the substance that gives skin its color. Pigmented lesions are characterized by the brown color of melanin and include freckles, solar lentigines, also known as sun spots or age spots, and café au lait birthmarks. Changes to the skin caused by abnormally large or numerous blood vessels located under the surface of the skin are called vascular lesions. Vascular lesions are characterized by blood vessels that are visible through the skin or that result in a red appearance of the skin. Vascular lesions may be superficial and shallow in the skin or deep in the skin. Shallow vascular lesions include small spider veins, port wine birthmarks, facial veins and rosacea, a chronic skin condition that causes rosy coloration and acne-like pimples on the face. Deep vascular lesions include large spider veins and leg veins.

People with undesirable skin conditions or unwanted hair growth often seek aesthetic treatments, including treatments using non-invasive laser and light-based technologies.

Non-Invasive Laser and Light-Based Aesthetic Treatments

A laser is a device that creates and amplifies a narrow, intense beam of light. Lasers have been used for medical and aesthetic applications since the 1960s. Intense pulsed light technology was introduced in the 1990s and uses flashlamps, rather than lasers, to generate multiple wavelengths of light with varying pulse durations, or time intervals, over which the energy is delivered.

By producing intense bursts of highly focused light, lasers and other light-based technologies selectively target hair follicles, veins or collagen in or below the dermis, as well as cells responsible for pigmentation in the epidermis. When the target absorbs sufficient energy, it is destroyed. The degree to which energy is absorbed in the skin depends upon the skin structure targeted—e.g., hair follicle or blood vessel—and the skin type—e.g., light or dark. Different types of lasers and other light-based technologies are needed to effectively treat the spectrum of skin types and conditions. As a result, an active aesthetic practice may require multiple laser or other light-based systems in order to offer treatments to its entire client base.

Different types of lasers are currently used for a wide range of aesthetic treatments. Each type of laser operates at its own wavelength, measured in nanometers, which corresponds to a particular emission and color in the light spectrum. The most common lasers used for non-invasive aesthetic treatments are:

- *Pulse dye lasers*—produce a yellow light that functions at a shallow penetration depth.
- *Alexandrite lasers*—produce a near infrared invisible light that functions with high power at a deep penetration depth.

- *Diode lasers*—produce a near infrared invisible light that functions at a deep penetration depth.
- *Nd:Yag lasers*—produce a near infrared invisible light that functions over a wide range of penetration depths.

In addition to selecting the appropriate wavelength for a particular application, laser and other light-based treatments require an appropriate balance among three other parameters to optimize safety and effectiveness for aesthetic treatments:

- energy level—the amount of light emitted to heat the target;
- pulse duration—the time interval over which the energy is delivered; and
- spot size—the diameter of the energy beam.

As a result of the wide spectrum of aesthetic applications, patient skin types and users of technology, customer purchasing objectives for aesthetic treatment systems are diverse. We believe that as aesthetic spas and non-traditional physician customers play increasingly important roles as purchasers of aesthetic treatment systems, the market for these products will become even more diverse. Specifically, we expect that owners of different types of aesthetic treatment practices will place different emphases on various system attributes, such as breadth of treatment applications, return on investment, upgradeability and price. Accordingly, we believe that there is significant market opportunity for a company that tailors its product offerings to meet the needs of a wide range of market segments.

Minimally Invasive Laser Treatments

Laser liposuction is a minimally invasive procedure that not only complements but augments liposuction. As the most popular cosmetic surgical procedure in 2007, liposuction was performed approximately 500,000 times in the United States.

Our Solution

We offer tailored customer solutions to address the market for non-invasive light-based aesthetic treatment applications, including hair removal, treatment of vascular lesions, skin rejuvenation through the treatment of shallow vascular lesions and pigmented lesions and temporary reduction of the appearance of cellulite and for minimally invasive procedures for LaserBodySculpting for the removal of unwanted fat. We believe our laser and other light-based systems are reliable, user friendly and easily incorporated into both physician practices and spas. We complement our product offerings with comprehensive and responsive service offerings, including assistance with training, aesthetic practice development consultation and product maintenance. As of December 31, 2007, we had sold more than 7,100 aesthetic treatment systems.

We believe that the following factors enhance our market position:

- *Broad Technology Base.* Our products are based on a broad range of technologies and incorporate different types of lasers, such as Alexandrite, pulse dye, Nd:Yag and diode, as well as intense pulsed light devices. We believe we are one of a few companies that currently offer aesthetic treatment systems using Alexandrite and pulse dye lasers, which are particularly well suited for some applications and skin types. The following table provides information regarding the principal energy sources used in laser and other light-based aesthetic treatments that we offer and the primary application of each of these energy sources. The table also indicates how many of the six largest competitors in our industry we believe also offer products using this energy source. See "—Competition" below. We base our belief as to the six largest competitors in our industry and their product offerings on public company filings and information available on company websites.

Energy Source	Type of Light/Wavelength	Principal Applications	Competitive Offerings	
			Cynosure	Six Largest Competitors
Pulse Dye Laser	Visible light (Yellow)(585/595 nm)	Vascular lesions, including shallow and deep lesions	X	1 of 6
Alexandrite Laser	Near infrared invisible light (755 nm)	Hair removal, particularly for light skin types	X	1 of 6
Diode Laser	Near infrared invisible light (805/940/980 nm)	Hair removal, particularly for light skin types Vascular lesions, particularly shallow lesions Temporary reduction in the appearance of cellulite	X	3 of 6
Nd:Yag Laser	Near infrared invisible light (1064 nm)	Hair removal, particularly for medium and dark skin types Vascular lesions, particularly deep lesions	X	5 of 6
Intense Pulsed Light . . .	Visible/Near infrared invisible light (400-950 nm)	Hair removal, all skin types Vascular lesions, particularly shallow lesions and pigmented lesions Temporary reduction in the appearance of cellulite	X	5 of 6
Multiple Energy Source Workstations . . . . . (incorporating two or more energy sources)	Multiple	Multiple	X	3 of 6

- *Expansive Portfolio of Aesthetic Treatment Systems.* We sell over 16 different aesthetic treatment systems so that customers can select the product best suited to their practice or business. Our product portfolio includes single energy source systems as well as workstations that incorporate two or more different types of lasers or light-based technologies. By offering multiple technologies and system alternatives at a variety of price points, we seek to provide customers with tailored solutions that meet the specific needs of their practices while providing significant flexibility in their level of investment.
- *Upgrade Paths Within Product Families.* We design our products to facilitate upgrading within product families. These upgrade paths provide our customers with the opportunity to add additional energy sources and handpieces, which provides our customers with technological flexibility as they expand their practices.

- *Global Presence.* We have offered our products in international markets for over 16 years, with approximately 36% of our revenue generated from product sales outside of North America in 2007. We target international markets through a direct sales force in four European countries, Japan and China and through international distributors in 44 other countries.
- *Strong Reputation Established Over 16-Year History.* We have been in the business of developing and marketing aesthetic treatment systems for over 16 years. As a result of this history, we believe the Cynosure brand name is associated with a tradition of technological leadership.

Our Business Strategy

Our goal is to become the worldwide leader in providing non-invasive and minimally invasive aesthetic treatment systems. The key elements of our business strategy to achieve this goal are to:

- *Offer a Full Range of Tailored Aesthetic Solutions.* We believe that we have one of the broadest product portfolios in the industry, with multiple product offerings incorporating a range of laser and light sources at various price points across many aesthetic applications. Our approach is designed to allow our customers to select products that best suit their client base, practice size and the types of treatments that they wish to offer. This allows us to address the needs of the traditional physician customer market as well as the growing non-traditional physician customer market. Many of our newer products can be upgraded to systems with greater functionality as our customers' practices expand.
- *Launch Innovative New Products and Technologies for Emerging Aesthetic Applications.* Our research and development team builds on our broad range of laser and light-based technologies to target unmet needs in significant aesthetic treatment markets. Since 2002, we have introduced 14 new products. We launched the *Apogee Elite* system, our flagship product for hair removal, in March 2004; the *Cynergy* system, our flagship product for the treatment of vascular lesions, in February 2005, and the *Affirm* system, our flagship product for anti-aging, in April 2006. In addition, we began to distribute the *TriActive LaserDermology* system, our flagship product for the temporary reduction of the appearance of cellulite, in North America in February 2004. In November 2006, we began to distribute the *Smartlipo* system, which provides a minimally invasive procedure for LaserBodySculpting for the removal of unwanted fat. We are also working on new technologies for other emerging aesthetic applications.
- *Provide Comprehensive, Ongoing Customer Service.* We support our customers with a worldwide service organization that includes 25 field service engineers in North America and 61 international field service engineers working directly for us or our international distributors. The field service engineers install our products and respond rapidly to service calls to minimize disruption to our customers' businesses. Most of our new products are modular in design to enable quick and efficient service and support. We plan to bolster our existing service infrastructure by establishing new training and inventory hubs in Europe and the Asia/Pacific region.
- *Generate Additional Revenue from Existing Customer Base.* We believe that there are opportunities for us to generate additional revenue from existing customers who are already familiar with our products. Many of our existing traditional and non-traditional customers may be purchasers of additional aesthetic treatment systems to address increasing treatment volumes or new treatment applications. We also expect that customers purchasing our new modular products will be candidates for technology upgrades to enhance the capabilities of their systems. In addition, two of our six flagship products, our *Affirm* and *Smartlipo* systems, contain consumable parts and we generate additional revenue on sales of these consumable parts to our existing customers. As we continue to grow our service organization, we are seeking to increase the percentage of our customers that enters into service contracts, which would provide additional recurring customer revenue.

Products

We offer a broad portfolio of aesthetic treatment systems that address a wide variety of applications.

The following table provides information concerning our flagship products and their applications. We use the flagship designation for our products that are our leading products for a particular application.

			Application								
	Laser/Light Source	Year Introduced	Hair Removal	Vascular Lesions	Skin Rejuvenation (1)	Pigmented Lesions	Temporary Reduction of Appearance of Cellulite	Acne	Tattoo Removal	Anti-Aging	LaserBody Sculpting and Removal of Unwanted Fat
Flagship Products:											
Apogee Elite	Alexandrite Nd:Yag	2004	Flagship	X	X	X					
Apogee 5500	Alexandrite	2004	X			X					
Acclaim 7000	Nd:Yag	2004	X	X	X	X					
Cynergy	Pulse Dye Nd:Yag	2005		Flagship	X	X					
Vstar	Pulse Dye	2000		X				X			
Acclaim 7000	Nd:Yag	2004	X	X	X						
TriActive LaserDermology(2)	Diode Laser	2004					Flagship				
Affirm	Nd:Yag Pulsed Light	2006								Flagship	
Smartlipo(2)	Nd:Yag	2006									Flagship
Accolade	Alexandrite	2008				Flagship			X		

(1) We consider skin rejuvenation to be the treatment of shallow vascular lesions and pigmented lesions to rejuvenate the skin's appearance.

(2) We distribute the *TriActive LaserDermology* and *Smartlipo* systems in North America pursuant to a distribution agreement with El.En.

System Components

Each of our systems consists of a control console and one or more handpieces. Our control consoles are each comprised of a graphical user interface, a laser or other light source, control system software and high voltage electronics. The graphical user interface allows the practitioner to set the appropriate laser or flashlamp parameters to meet the requirements of a particular application and patient. The laser or other light source consists of electronics, a visible aiming beam, a focusing lens and a laser or flashlamp. Using the graphical user interface, the practitioner can independently adjust the system's power level and pulse duration to optimize the desired treatment's safety and effectiveness. The graphical user interface on our multiple energy workstations also allows the practitioner to change energy sources with the press of a button. The graphical user interfaces on our intense pulsed light systems offer practitioners a choice between using programmed preset treatment settings that address a variety of skin types and treatment options or manually adjusting the energy level and pulse duration settings. The control system software communicates the operator's instructions from the graphical user interface to the system's components and manages system performance and calibration.

The handpieces on our laser systems deliver the laser energy through a maneuverable optical fiber to the treatment area. These handpieces weigh approximately eight ounces and are ergonomically designed to allow the practitioner to use the system with one hand and without becoming fatigued. Other features of our laser system handpieces include:

- interchangeable components that permit the practitioner to easily adjust the spot size; and
- an integrated aiming beam of harmless visible light that allows the practitioner to verify the treatment area, thereby reducing the risk of unintended skin damage and potentially reducing treatment time.

The handpieces for our intense pulsed light systems consist of the flashlamp, a wavelength filter and, on some models, an integrated flashlamp cooling system. These handpieces weigh approximately two pounds and also are ergonomically designed to be operated with one hand.

Two of our six flagship products, our *Affirm* and *Smartlipo* systems, contain consumable parts. The *Affirm* system contains a highly durable micro lens array tip, which delivers the laser energy employed that can treat an average of ten treatment areas. We currently offer three different micro lens array tips, which cover a variety of treatment areas. The *Smartlipo* system contains a consumable laser fiber that delivers the laser energy directly to subcutaneous fat cells-causing them to rupture.

Practitioners generally use our laser systems in combination with a cooling system. We offer our customers our *SmartCool* treatment cooling system, which we purchase from a third party supplier and sell as a private label product under the Cynosure *SmartCool* brand. Our *SmartCool* product has nine variable settings and allows the practitioner to provide a continuous flow of chilled air before, during and after treatment to cool and comfort the patient's skin. The *SmartCool* handpiece, which is specially designed for use with our laser systems, interlocks with the laser handpiece. In contrast to some competitive cooling systems, there are no disposable supplies required to use our *SmartCool* system. In North America, our *SmartCool* system is generally packaged and sold with our laser aesthetic treatment systems, and nearly all of our North American customers purchase a *SmartCool* system when they purchase one of our laser aesthetic treatment systems. Outside of North America, our customers either purchase our *SmartCool* system when they purchase one of our aesthetic treatment systems or they purchase another cooling system from a third party supplier.

Applications

Practitioners use our products to perform a variety of non-invasive procedures to remove hair, treat vascular and pigmented lesions, rejuvenate skin through the treatment of shallow vascular lesions and pigmented lesions, temporarily reduce the appearance of cellulite, treat wrinkles, skin texture, skin discoloration and skin tightening through tissue coagulation, and to perform minimally invasive procedures for LaserBodySculpting for the removal of unwanted fat. These applications of our products are described below.

Hair Removal. In a typical laser or pulsed light hair removal treatment, the target area is first cleaned and shaved. The practitioner then selects appropriate laser or pulsed light parameters based on the patient's skin and hair types and pre-cools the treatment area. The practitioner next applies the handpiece to the target area and delivers laser or pulsed light energy to the selected area. The laser or pulsed light removes hair by directing energy to the target melanin pigment of the hair follicle, destroying the hair follicle without harming the surrounding skin. This procedure can last from a few minutes to one hour depending on the size of the treatment area and laser or pulsed light spot size. Chilled air is applied to the treatment area on a continuous basis to cool and comfort the patient's skin. Generally, for permanent reduction, hair removal requires three to six treatments spaced four to six weeks apart.

Our *Apogee Elite* workstation is our flagship product for hair removal. It is a two-in-one laser system that contains both an Alexandrite laser, which is best suited for hair removal for patients with light skin types, and an Nd:Yag laser, which is best suited for hair removal for patients with medium and dark skin types or tanned skin. The practitioner can switch between these two energy sources simply by pressing a button on the system console. Features of the *Apogee Elite* system include:

- A wide range of separately adjustable power and pulse duration settings. This allows the practitioner to select the best settings for safe and efficient hair removal depending on the patient's skin and hair type. Some competitive systems do not permit pulse duration adjustment, which we believe may reduce the effectiveness of the treatment, particularly for thicker hair.
- A large, 15 millimeter spot size and a laser beam that distributes energy evenly over the entire treatment area. This allows the practitioner to treat a targeted area in an efficient manner. Some

competitive systems have smaller spot sizes or beams that concentrate the energy in the middle of the treatment area of each pulse of light, which requires more overlap of the treatment areas of the individual pulses of light to achieve an effective result.

- A rapid pulse rate. This permits the practitioner to cover the treatment area quickly, which is particularly important when removing hair from large areas, such as backs and legs.

In addition to the *Apogee Elite* system, each of our *Apogee 5500,* and *Acclaim 7000* systems can be used for hair removal.

Treatment of Vascular Lesions. To treat vascular lesions the practitioner generally first pre-cools the target area and then applies the system handpiece to deliver laser energy to the treatment area. Depending on the size of the treatment area, procedures last between 20 and 30 minutes. In some cases, a topical anesthetic is applied to the treatment area to minimize pain. For spider veins, redness and rosacea, patients generally receive between two and four treatments spaced over two to three weeks. For port wine birthmarks, patients may receive ten or more treatments.

Our *Cynergy* workstation is our flagship product for the treatment of vascular lesions. The *Cynergy* system combines a pulse dye laser, which is best suited for treating shallow vascular lesions, such as port wine birthmarks, facial veins and rosacea, and an Nd:Yag laser, which is best suited for treating large or deep veins, such as leg veins. The practitioner can switch between these two energy sources simply by pressing a button on the system console. Other features of the *Cynergy* system include:

- A wide range of separately adjustable power and pulse duration settings. This allows the practitioner to select the best settings for safe and efficient treatment depending on the particular type and depth of the vascular lesion to be treated.
- One of the most powerful pulse dye lasers currently available in the aesthetic treatment system market. The power of this laser allows a practitioner to provide treatment with a spot size that is larger than would be effective with a less powerful laser, thereby enhancing treatment efficiency.
- *SixPulse*(TM) technology in the pulse dye laser, which distributes the power of one long pulse of energy into six micro pulses. This allows the practitioner to deliver more energy with less patient discomfort.
- A choice of five different spot sizes that are easily selected through the use of interchangeable headpiece components. This allows the practitioner to select the appropriate spot size for the particular vascular lesion to be treated. For example, a large spot size is generally used for a large leg vein, while a small spot size is normally used for facial veins.

In March 2006, we obtained FDA clearance for our innovative *Multiplex*(TM) energy delivery system that is now available on the *Cynergy* system. Our *Multiplex* system mixes the energy from the two lasers included in *Cynergy* system by quickly following a pulse of energy from the pulse dye laser with a pulse of energy from the Nd:Yag laser. Clinical studies that we conducted have shown that *Multiplex* delivery allows for more efficient treatment of vascular lesions by reducing the amount of laser power required and allowing the laser energy to penetrate deeper into the target.

In addition to the *Cynergy* system, each of our *Apogee Elite, Acclaim 7000,* and *VStar* systems can be used for the treatment of vascular lesions.

Anti-Aging. We believe the marketplace is moving towards a more non-invasive system with anti-aging procedures, including wrinkle reduction, pigmentation, redness and overall skin rejuvenation. Our *Affirm* was created to address the needs of the anti-aging demand. Anti-aging treatments were historically performed by physicians who could only target one condition and one skin layer during each treatment. Previously, patients often faced longer, more painful procedures that penetrated into the dermal layers and could damage potentially healthy skin.

Our *Affirm* system is our flagship product for anti-aging, including treatments for wrinkles, skin texture, skin discoloration and skin tightening through tissue coagulation. The *Affirm* system is the first micro-rejuvenation system, which includes our patent pending mid-infrared Combined Apex Pulse(TM), or CAP, delivery system and Xenon Pulsed Light, or XPL, technology in one system. Our proprietary CAP technology stimulates collagen production throughout the entire treatment area. Through precise thermal manipulation of the epidermal and dermal tissue, it remodels collagen through the papillary dermis to promote collagen production and skin tightening. The laser energy is delivered through a durable and disposable tip that can treat an average of ten treatment areas. The XPL portion of the system effectively eradicates dyschromia, a common condition associated with aging skin. The XPL provides enhanced outcomes by targeting superficial pigments, veins and the blush of rosacea associated with sun damaged skin.

In 2007, we expanded our anti-aging aesthetic solution to include a new 1320 nm wavelength Nd:YAG laser. The *Affirm* product family now incorporates three energy sources and the new deep-heating component provided by the new 1320 nm wavelength Nd:YAG laser allows for tissue tightening, as a result of tissue coagulation, which complements the current 1440 nm Nd:YAG laser for fractional micro-rejuvenation and the Xenon Pulsed Light system for discoloration. We began shipping these new upgradeable systems in mid-2007. Customers can also purchase the multi-energy *Affirm* workstations with three separate energy sources as well as three different lens arrays that encompass the full range of anti-aging applications in a single platform.

Skin Rejuvenation. Skin rejuvenation involves the treatment of shallow vascular lesions and pigmented lesions to rejuvenate the skin's appearance. In a skin rejuvenation procedure, the practitioner applies the system handpiece to the target area and delivers laser or pulsed light energy. The energy destroys the shallow vascular lesions and pigmented lesions and rejuvenates the skin's appearance without damage to the treated or surrounding area through the improvement in skin texture and reduction or elimination of skin irregularities. Cooling is generally not required. Patients typically receive between four to six treatments of approximately 30 minutes each. Treatments are spaced two to four weeks apart.

Each of our *Apogee Elite*, *Acclaim 7000* and *Cynergy* systems can be used for skin rejuvenation through the treatment of shallow vascular lesions and pigmented lesions.

Temporary Reduction of Appearance of Cellulite. Cellulite is a deposit of fat that causes a dimple or other uneven appearance of the skin on women, typically around the thighs, hips and buttocks. According to published reports, an estimated 80% of women have some degree of cellulite. In a treatment for the temporary reduction of the appearance of cellulite, the practitioner applies the multifunction handpiece to deliver diode laser energy, as well as suction and manipulation therapy, to the treatment area. The laser energy and suction and manipulation therapy enhance micro-circulation in the area of the cellulite. Treatment for the temporary reduction in the appearance of cellulite requires a series of treatments of approximately 30 to 45 minutes each, depending on the treatment area and patient response.

Our *TriActive LaserDermology* system is our flagship product for temporarily reducing the appearance of cellulite. The *TriActive* system contains six low-energy diode lasers, mechanical massage and suction features and localized cooling. The *TriActive* system is one of only two light-based systems, and the only laser-based system, cleared by the FDA for use for the temporary reduction in the appearance of cellulite. In addition, the FDA has cleared *TriActive* system as an over-the-counter device, for sale and use without physician supervision, because its diode lasers are sealed and do not pose a risk of exposure to operators' eyes. We believe that *TriActive* system is the only light-based system for this application that has been so cleared by the FDA, which significantly facilitates our marketing of *TriActive* system to the growing aesthetic spa market.

LaserBodySculpting for the Removal of Unwanted Fat. Liposuction and body sculpting procedures is the number one procedure to remove or reduce fat cells.

Our *Smartlipo* system is our flagship product for LaserBodySculpting for the removal of unwanted fat. The *Smartlipo* system was the first laser lipolysis system to offer a minimally invasive procedure for the removal of unwanted fat. The *Smartlipo* LaserBodySculpting(SM) procedure enables aesthetic surgeons to treat localized deposits of fat. The *Smartlipo* LaserBodySculpting procedure is performed by inserting a small cannula, or metal tube, containing a laser fiber and placing it under the skin in direct contact with the treatment area. The laser's energy causes the fat cells to rupture and melt. In addition, the laser's energy promotes collagen shrinkage and causes a tissue tightening effect. LaserBodySculpting is a minimally invasive procedure; therefore, it can be performed under local anesthesia with minimal trauma in comparison to alternative liposuction procedures.

In 2007, we released two new *Smartlipo* workstations, the 10-watt and the 18-watt *Smartlipo* workstations, that are intended for high-volume aesthetic laser practices, allowing a physician to reduce patient treatment times for laser-assisted liposuction procedures. The 10-watt and 18-watt *Smartlipo* workstations are available as a standalone unit or as an upgrade to existing systems.

In February 2008, we introduced our *Accolade* system, which is our flagship solution for the removal of pigmented lesions. The *Accolade* is a high powered 755 nm, Q-switched Alexandrite laser. The unique combination of various spot sizes and the laser's high repetition rates allow for rapid treatment. The initial target markets for *Accolade* includes Japan, Korea and China, where dermal lesions such as Nevus of Ota and Nevus of Ito are common.

Sales and Marketing

We sell our aesthetic treatment systems to the traditional physician customer base of dermatologists and plastic surgeons as well as to the increasing number of non-traditional physician customers who are providing aesthetic services using laser and light-based technology. Non-traditional physician customers can include primary care physicians, obstetricians, gynecologists, ophthalmologists and ear, nose and throat specialists.

We target potential customers through office visits, trade shows and trade journals. We also conduct clinical workshops featuring recognized expert panelists and opinion leaders to promote existing and new treatment techniques using our products. We believe that these workshops enhance customer loyalty and provide us with new sales opportunities. We also use direct mail programs to target specific segments of the market that we seek to access, such as members of medical societies and attendees at meetings sponsored by medical societies or associations. In addition, we have recently implemented a public relations program that has resulted in sales opportunities based on our products being featured in several popular U.S. women's magazines.

We do not provide financing to our customers to purchase our products. If a potential customer requests financing, we refer the customer to third party financing sources.

Physician Sales

We sell our products to physicians in North America through a direct sales force. Outside of North America, we sell our products to physicians through a direct sales force in four European countries, Japan and China and through independent distributors in 44 other countries.

We conduct our own international sales and service operations through wholly-owned subsidiaries in the United Kingdom, France, Germany, Spain, Japan and China. We seek distributors in international markets where we do not believe that a direct sales presence is warranted or feasible. In those markets, we select distributors that have extensive knowledge of our industry and their local markets. Our distributors sell, install and service our products. We require our distributors to invest in service training and equipment, to stock and supply maintenance and service parts for our systems, to attend exhibitions and industry meetings and, in some instances, to commit to minimum sales amounts to gain or retain exclusivity. Currently, we have written distribution agreements with 18 of our 19 third party distributors. Generally, the written agreements with our distributors have terms of between one and two years.

Service and Support

We support our customers with a range of services, including installation and product training, business and practice development consulting and product service and maintenance. In North America, our field service organization has 25 field service engineers. Outside of North America, our sales and service subsidiaries and our trained distributors employ 61 field service engineers.

In connection with direct sales of our aesthetic treatment systems, we arrange for the installation of the system and initial product training. Generally, installation and initial training takes less than three hours. The installation is conducted by our field service engineers. We offer a service that is particularly appealing to the non-traditional physician customer and aesthetic spa segments of the market, which have less familiarity with the business aspects of laser and light-based aesthetic treatments than dermatologists and cosmetic surgeons. The cost of installation and initial training for North American purchasers are all included in the purchase price of our systems. We also offer for an additional charge a more comprehensive package of services from the third party consultant.

We strive to respond to all service calls within 24 hours to minimize disruption of our customers' businesses. We have designed our new products in a modular fashion to enable quick and efficient service and support. Specifically, we build these products with several separate components that can easily be removed and replaced when the product is being serviced. We provide initial warranties on our products to cover parts and service, and we offer extended warranty packages that vary by type of product and level of service desired. Our base warranty covers parts and service for one year. We offer extended warranty arrangements through service plans. We believe that we have a significant opportunity to increase our recurring customer revenues by increasing the percentage of our customers that enter into service contracts for our systems.

Research and Development

Our research and development team consists of 29 employees with a broad base of experience in lasers and optoelectronics. Our research and development team works closely with opinion leaders and customers, both individually and through our sponsored seminars, to understand unmet needs and emerging applications in the field of aesthetic skin treatments and to develop new products and improvements to our existing products. They also conduct and coordinate clinical trials of our products. Our research and development team builds on the significant base of patented and proprietary intellectual property that we have developed in the fields of laser and other light-based technologies since our inception in 1991.

Our research and development expenses were approximately $6.8 million in 2007, $4.7 million in 2006 and $3.2 million in 2005, none of which was customer sponsored. We expect our research and development expenditures to increase as we continue to devote resources to research and develop new products and technologies.

Manufacturing and Raw Materials

We manufacture all of our products, other than the *TriActive LaserDermology* and *Smartlipo* systems, which are manufactured by El.En. and which we sell and market under our distribution agreement with El.En. We manufacture our products with components and subassemblies purchased from third party suppliers. Accordingly, our manufacturing operations consist principally of assembly and testing of our systems and integration of our proprietary optics and software.

We design our products, including our *Apogee, Cynergy, Acclaim* and *VStar* product families, so that they are built in a modular fashion using fewer components. This approach enables us to manufacture our products more efficiently.

We purchase many of our components and subassemblies from third party manufacturers on an outsourced basis. We use one third party to assemble and test many of the components and subassemblies for our *Affirm*, *Apogee*, *Cynergy*, *Acclaim* and *VStar* product families. We also depend exclusively on sole source suppliers for Alexandrite rods, which we use in the manufacture of our *Apogee* products, and for our *SmartCool* treatment cooling systems.

We do not have long-term contracts with our third party manufacturers or sole source suppliers. We generally purchase components and subassemblies as well as our other supplies on a purchase order basis. If for any reason, our third party manufacturers or sole source suppliers are not willing or able to provide us with components, subassemblies or supplies in a timely fashion, or at all, our ability to manufacture and sell many of our products could be impaired. To date, we have been able to obtain adequate outsourced manufacturing services and supplies of Alexandrite rods and air cooling systems from our third party manufacturers and suppliers in a timely manner. We believe that over time alternative component and subassembly manufacturers and suppliers can be identified if our current third party manufacturers and suppliers fail to fulfill our requirements.

El.En. Commercial Relationship

The *TriActive LaserDermology* and *Smartlipo* systems sold by us were developed, and associated intellectual property rights are owned, by El.En. El.En. manufactures, and we distribute, these products pursuant to distribution agreements between us and El.En. These agreements provide us with exclusive distribution rights in the United States and Canada for the *TriActive LaserDermology* and *Smartlipo* systems. The transfer prices for products that we currently distribute under the agreements are specified in the agreement; however, they may be changed by El.En. at its discretion upon 30 days' notice.

El.En. is required to provide us with training, marketing and other sales support for the products we distribute under these agreements. We are required to use best efforts to sell and promote these products, and we are responsible for obtaining and maintaining regulatory approvals for them. If El.En. wishes to discontinue producing products that we distribute, it must make reasonable efforts to provide us with one year's notice of its plan to do so.

The distribution agreement for the *Smartlipo* systems expires in 2014. The distribution agreement relating to the *TriActive LaserDermology* system will automatically renew for additional one-year terms unless either party provides notice of termination at least six months prior to the expiration of the initial term or any subsequent renewal term. We or El.En. may terminate the distribution agreements at any time based upon material uncured breaches by, or the insolvency of, the other party. In addition, El.En. may terminate the distribution agreement for the *TriActive LaserDermology* and *Smartlipo* systems if we do not meet annual minimum purchase obligations specified in the agreements.

Patents, Proprietary Technology and Trademarks

Our success depends in part on our ability to obtain and maintain proprietary protection for our products, technology and know-how, to operate without infringing the proprietary rights of others and to prevent others from infringing our proprietary rights. Our policy is to seek to protect our proprietary position by, among other methods, filing United States and foreign patent applications related to our proprietary technology, inventions and improvements that are important to the development of our business. We also rely on trade secrets, know-how, continuing technological innovation and in-licensing opportunities to develop and maintain our proprietary position.

As of December 31, 2007, we owned a total of 38 United States patents, as well as foreign counterparts to 21 of these patents. Our patent portfolio includes patents and patent applications with claims directed to:

- the design and method of use and operation of our pulse dye laser systems;
- the design and method of use and operation of our Alexandrite laser systems for hair removal;
- our Multiplex energy delivery system for our pulse dye lasers; and
- the design of endoscopic laser and light delivery systems.

The expiration dates for our issued United States patents range from 2013 to 2023. Additionally, El.En. has applied for a patent covering the methods of use and operation of the *TriActive LaserDermology* system. We do not consider any single patent or patent application that we hold to be material to our business.

The patent positions of companies like ours are generally uncertain and involve complex legal and factual questions. Our ability to maintain and solidify our proprietary position for our technology will depend on our success in obtaining effective patent claims and enforcing those claims once granted. We do not know whether any of our patent applications or those patent applications that we license will result in the issuance of any patents. Our issued patents and those that may issue in the future, or those licensed to us, may be challenged, invalidated or circumvented, which could limit our ability to stop competitors from marketing related products or shorten the term of patent protection that we may have for our products. In addition, the rights granted under any issued patents may not provide us with competitive advantages against competitors with similar technology. Furthermore, our competitors may independently develop similar technologies or duplicate any technology developed by us. Because of the extensive time required for development, testing and regulatory review of a potential product, it is possible that, before any of our products under development can be commercialized, any related patent may expire or remain in force for only a short period following commercialization, thereby reducing any advantage of the patent.

On November 6, 2006, we entered into a patent cross-license agreement with Palomar. Under the cross-license agreement, we obtained a non-exclusive license to integrate into our products certain hair removal technology covered by specified U.S. and foreign patents held by Palomar and Palomar obtained a non-exclusive license under certain U.S. and foreign patents held by us. In November 2006, we made a payment to Palomar of $10 million for royalties related to sales prior to October 1, 2006 of hair removal-only systems. In connection with this agreement, we also agreed to pay royalties to Palomar on future sales of certain hair removal-only products. The royalty rate for future sales of hair removal products will range from 3.75% to 7.5% of net sales beginning October 1, 2006, depending upon product configuration and the number of energy sources. Our revenue from systems that do not include hair removal capabilities and revenue from service is not subject to any past or future royalties under this agreement.

We rely, in some circumstances, on trade secrets to protect our technology. Trade secrets, however, are difficult to protect. We seek to protect our proprietary technology and processes, in part, by confidentiality agreements with our employees, consultants, scientific advisors and other contractors. These agreements may be breached, and we may not have adequate remedies for any breach. In addition, our trade secrets may otherwise become known or be independently discovered by competitors. To the extent that our employees, consultants or contractors use intellectual property owned by others in their work for us, disputes may arise as to the rights in related or resulting know-how and inventions.

We use trademarks on nearly all of our products and believe that having distinctive marks is an important factor in marketing our products. We have registered our *Cynosure*(R), *Apogee*(R), *PhotoGenica*(R) and *SmartCool*(R) marks, among others, in the United States. Our other trademarks include *Affinity*(TM), *Acclaim*(TM), *Apogee Elite*(TM), *Cynergy*(TM), *CynosureSpa*(TM), *PhotoLight*(TM), *PhotoSilk*(TM), *PhotoSilk Plus*(TM), *Smartlipo*(TM), *Affirm*(TM) and *LaserDermology*(SM). We have also registered some of our marks in

a number of foreign countries. In addition, El.En. has registered the *TriActive*(R) mark in the United States. Although we have a foreign trademark registration program for selected marks, we may not be able to register or use such marks in each foreign country in which we seek registration.

Competition

Our industry is subject to intense competition. Our products compete against laser and other light-based products offered by public companies, such as Candela Corporation, Cutera, Inc., Lumenis Ltd., Palomar Medical Technologies, Inc., Syneron Medical Ltd. and Thermage, Inc., as well as several smaller specialized private companies, such as Reliant Technology, Inc. and Alma Lasers, Ltd. Some of these competitors have greater financial and human resources than we do and have established reputations, as well as worldwide distribution channels and sales and marketing capabilities that are larger and more established than ours. Additional competitors may enter the market, and we are likely to compete with new companies in the future. Our products also compete against non-light-based medical products, such as BOTOX(R) and collagen injections, and surgical and non-surgical aesthetic procedures, such as face lifts, chemical peels, abdominoplasty, liposuction, microdermabrasion, sclerotherapy and electrolysis.

Competition among providers of aesthetic laser and other light-based products is characterized by significant research and development efforts and rapid technological progress. There are few barriers that would prevent new entrants or existing competitors from developing products that would compete directly with ours. There are many companies, both public and private, that are developing innovative devices that use both light-based and alternative technologies for aesthetic and medical applications. Accordingly, our success depends in part on developing and commercializing new and innovative applications of laser and other light-based technology and identifying new markets for and applications of existing products and technology.

To compete effectively, we have to demonstrate that our products are attractive alternatives to other devices and treatments by differentiating our products on the basis of performance, reputation, quality of customer support and price. Breadth of product offering is also important. We believe that we perform favorably with respect to each of these factors. However, we have encountered and expect to continue to encounter potential customers who, due to pre-existing relationships with our competitors, are committed to, or prefer the products offered by these competitors. Potential customers also may decide not to purchase our products, or to delay such purchases, based on a decision to recoup the cost of expensive products that they may have already purchased from our competitors. In addition, we expect that competitive pressures may result in price reductions and reduced margins over time for our products.

Government Regulation

Our products are medical devices subject to extensive and rigorous regulation by the U.S. Food and Drug Administration, or FDA, as well as other regulatory bodies. FDA regulations govern the following activities that we perform and will continue to perform to ensure that medical devices distributed domestically are safe and effective for their intended uses.

FDA's Regulation of Manufacturing

The FDA requires that we manufacture our products in accordance with its Quality System Regulation, or QSR. The QSR covers the methods and documentation of the design, testing, control, manufacturing, labeling, quality assurance, packaging, storage and shipping of our products. The FDA enforces the QSR through periodic unannounced inspections. Based on our communication with the FDA, we expect an inspection of our new facility to occur in the near future.

Our failure to maintain compliance with the QSR requirements could result in the shut down of, or restrictions on, our manufacturing operations and the recall or seizure of our products, which would have a

material adverse effect on our business. In the event that one of our suppliers fails to maintain compliance with our quality requirements, we may have to qualify a new supplier and could experience manufacturing delays as a result.

We maintain quality assurance and quality management certifications to enable us to market our products in the member states of the European Union, the European Free Trade Association and some countries that have entered into Mutual Recognition Agreements with the European Union. In November 1998, our former facility was awarded the ISO 9001 and EN 46001 certifications. In October 2003, we received our ISO 9001 updated certification as well as our certification for ISO 13485, which replaced our EN 46001 certification.

FDA's Premarket Clearance and Approval Requirements

Unless an exemption applies, each medical device we wish to distribute commercially in the United States requires either prior 510(k) clearance or premarket approval from the FDA. The FDA classifies medical devices into one of three classes. Devices deemed to pose lower risks are placed in either class I or II, which requires the manufacturer to submit to the FDA a premarket notification requesting permission to distribute the device commercially. This process is generally known as 510(k) clearance. Class I devices are subject to general controls such as labeling and adherence to FDA's QSR. Class II devices are subject to special controls such as performance standards and FDA guidelines as well as general controls. The FDA exempts some low risk devices from premarket notification requirements and the requirement of compliance with certain provisions of the QSR. The FDA places devices in class III, requiring premarket approval, if insufficient information exists to determine that the application of general controls or special controls are sufficient to provide reasonable assurance of safety and effectiveness and they are life-sustaining, life-supporting or implantable devices, or devices deemed not substantially equivalent to a previously cleared 510(k) device or to a "preamendment" class III device in commercial distribution before May 28, 1976, for which premarket approval applications have not been required. All of our current products are class II devices. Both premarket notifications and premarket approval applications when submitted to FDA must be accompanied by a user fee, unless exempt.

510(k) Clearance Pathway

When a 510(k) clearance is required, we must submit a premarket notification to the FDA demonstrating that our proposed device is substantially equivalent to a previously cleared 510(k) device or a device that was in commercial distribution before May 28, 1976 for which the FDA has not yet called for the submission of premarket approval applications, or premarket approval. By regulation, the FDA must clear or deny a 510(k) premarket notification within 90 days of submission of the application. As a practical matter, clearance often takes significantly longer. The FDA may require further information, including clinical data, to make a determination regarding substantial equivalence.

Laser devices used for aesthetic procedures, such as hair removal, have generally qualified for clearance under 510(k) procedures.

Premarket Approval Pathway

If the device cannot be cleared through the 510(k) process, the sponsor must submit a premarket approval application, which is known as a PMA. The sponsor must support the PMA with extensive data, including but not limited to, technical, preclinical, clinical trials, manufacturing and labeling to demonstrate to the FDA's satisfaction the safety and effectiveness of the device.

No device that we have developed has required premarket approval, nor do we currently expect that any future device or indication will require premarket approval.

Product Modifications

After a device receives 510(k) clearance or a PMA approval, any modification that could significantly affect its safety or effectiveness, or that would constitute a major change in its intended use, will require a new clearance or approval. The FDA requires each manufacturer to make this determination initially, but the FDA can review any such decision and can disagree with a manufacturer's determination. We have modified aspects of various products since receiving regulatory clearance and believe that new 510(k) clearances are not required for these modifications. If the FDA disagrees with our determination not to seek a new 510(k) clearance or PMA approval, the FDA may retroactively require us to seek 510(k) clearance or premarket approval. The FDA could also require us to cease marketing and distributing the modified device, and the recall any sold devices, until 510(k) clearance or premarket approval is obtained. Also, in these circumstances, we may be subject to significant regulatory fines or penalties.

Clinical Trials

We perform clinical trials to provide data to support the FDA clearance process for our products and for use in our sales and marketing efforts. Human clinical studies are generally required in connection with approval of class III devices and may be required for clearance of class I and II devices. When FDA clearance or approval of a device requires human clinical trials, and if the device presents a "significant risk," as defined by the FDA, to human health, the FDA requires the device sponsor to file an investigational device exemption, or IDE, application with the FDA and obtain IDE approval prior to commencing the human clinical trials. The sponsor must support the IDE application with appropriate data, such as animal and laboratory testing results, showing that it is safe to test the device in humans and that the testing protocol is scientifically sound. The sponsor also must obtain approval from the institutional review board overseeing the clinical trial.

To date, we have not submitted any IDEs because we believe our devices present only "non-significant" risks and, therefore, do not require IDE submission to the FDA. Instead, only institutional review board approval is required. Future clinical trials of our products may require that we submit and obtain approval of an IDE from the FDA prior to commencing clinical trials. The FDA, and the institutional review board at each institution at which a clinical trial is being performed, may suspend a clinical trial at any time for various reasons, including a belief that the subjects are being exposed to an unacceptable health risk.

All clinical investigations of devices to determine safety and effectiveness must be conducted in accordance with the FDA's IDE regulations which govern investigational device labeling, prohibit promotion of the investigational device, and specify an array of recordkeeping, reporting and monitoring responsibilities of study sponsors and study investigators. Clinical trials must further comply with FDA regulations for institutional review board approval and for informed consent. Required records and reports are subject to inspection by the FDA. The results of clinical testing may be unfavorable or inconclusive or, even if the intended safety and effectiveness success criteria are achieved, may not be considered sufficient for the FDA to grant approval or clearance of a product. The commencement or completion of any of our clinical trials may be delayed or halted, or be inadequate to support approval of a PMA application, or 510(k) clearance, for numerous reasons, including, but not limited to, the following:

- patients do not enroll in clinical trials or there is not patient follow-up at the rate we expect;
- patients do not comply with trial protocols;
- patients experience adverse side effects;
- institutional review boards and third party clinical investigators may delay or reject our trial protocol;
- third party clinical investigators decline to participate in a trial or do not perform a trial on our anticipated schedule or consistent with the clinical trial protocol, good clinical practices, or other FDA requirements;

- regulatory inspections of our clinical trials or manufacturing facilities, which may, among other things, require us to undertake corrective action or suspend or terminate our clinical trials or invalidate our clinical trials; and
- changes in governmental regulations or administrative actions.

Our clinical trials may not generate favorable data to support any PMA or 510(k), and we may not be able to obtain such approvals or clearances on a timely basis, or at all. Delays in receipt of or failure to receive such approvals or clearances or failure to comply with existing or future regulatory requirements would have a material adverse effect on our business, financial condition and results of operations. Even if granted, the approvals or clearances may include significant limitations on the intended use and indications for use for which our products may be marketed.

Clinical studies conducted on 510(k) cleared devices, when used or investigated in accordance with the devices' labeled instructions, are exempt from most of the FDA's IDE requirements.

Pervasive and Continuing Regulation

After a device is placed on the market, numerous regulatory requirements apply. These include:

- establishment registration and device listing;
- the quality system regulation, which requires manufacturers, including third-party manufacturers, to follow stringent design, testing, control, documentation and other quality assurance procedures during all aspects of the manufacturing process;
- labeling regulations and FDA prohibitions against the promotion of products for uncleared, unapproved or "off-label" uses, and other requirements related to promotional activities;
- medical device reporting regulations, which require that manufacturers report to the FDA if their device may have caused or contributed to a death or serious injury or malfunctioned in a way that would likely cause or contribute to a death or serious injury if the malfunction were to recur;
- corrections and removal reporting regulations, which require that manufacturers report to the FDA field corrections and product recalls or removals if undertaken to reduce a risk to health posed by the device or to remedy a violation of the Federal Food, Drug, and Cosmetic Act that may present a risk to health; and
- post-market surveillance regulations, which apply when necessary to protect the public health or to provide additional safety and effectiveness data for the device.

The FDA may require us to maintain a system for tracking our products through the chain of distribution to the patient level. The FDA has broad post-market and regulatory enforcement powers. We are subject to unannounced inspections by the FDA to determine our compliance with the QSR and other regulations. These inspections may include the manufacturing facilities of our subcontractors. Thus, we must continue to spend time, money and effort to maintain compliance. The FDA has inspected our current manufacturing facility in September 2005 and we believe that we are in substantial compliance with the QSR. Since 1994, we have received five untitled letters from the FDA regarding alleged violations caused by our promotional activities. We have responded to these letters and the FDA found our responses acceptable.

We are also regulated under the Radiation Control for Health and Safety Act, which requires laser products to comply with performance standards, including design and operation requirements. The law also requires manufacturers to certify in product labeling and in reports to the FDA that their products comply with all such standards. The law and applicable federal regulations also require laser manufacturers to file new product and annual reports, maintain manufacturing, testing and sales records, and report product defects. Various warning labels must be affixed and certain protective devices installed, depending on the class of the product.

Failure to comply with applicable regulatory requirements can result in enforcement action by the FDA, which may include any of the following sanctions:

- untitled letters, warning letters, fines, injunctions, consent decrees and civil penalties;
- repair, replacement, refunds, recall or seizure of our products;
- operating restrictions, partial suspension or total shutdown of production;
- refusing or delaying our requests for 510(k) clearance or premarket approval of new products or new intended uses;
- withdrawing 510(k) clearance or premarket approvals that are already granted; and
- criminal prosecution.

The FDA also has the authority to require us to repair, replace or refund the cost of any medical device that we have manufactured or distributed. If any of these events were to occur, they could have a material adverse effect on our business.

We are also subject to a wide range of federal, state and local laws and regulations, including those related to the environment, health and safety, land use and quality assurance. We believe that compliance with these laws and regulations as currently in effect will not have a material adverse effect on our capital expenditures, earnings and competitive and financial position.

International

International sales of medical devices are subject to foreign governmental regulations, which vary substantially from country to country. The time required to obtain clearance or approval by a foreign country may be longer or shorter than that required for FDA clearance or approval, and the requirements may be different.

The primary regulatory environment in Europe is that of the European Union, which consists of 27 countries encompassing most of the major countries in Europe. The European Union has adopted numerous directives, and European Standardization Committees have promulgated voluntary standards, regulating the design, manufacture, clinical trials, labeling and adverse event reporting for medical devices. Devices that comply with the requirements of a relevant directive will be entitled to bear CE conformity marking, indicating that the device conforms to the essential requirements of the applicable directives and, accordingly, can be commercially distributed throughout the member states of the European Union and the member states of the European Free Trade Association, including Switzerland.

The method of assessing conformity varies depending on the type and class of the product, but normally involves a combination of self-assessment by the manufacturer and a third party assessment by a Notified Body, an independent and neutral institution appointed by a country to conduct the conformity assessment. This third party assessment may consist of an audit of the manufacturer's quality system and specific testing of the manufacturer's device. An assessment by a Notified Body in one member state of the European Union or the European Free Trade Association is required in order for a manufacturer to distribute the product commercially throughout these countries. ISO 9001 and ISO 13845 certification are voluntary harmonized standards. Compliance establishes the presumption of conformity with the essential requirements for a CE Marking. In November 1998, our former facility was awarded the ISO 9001 and EN 46001 certifications. In October 2003, we received our ISO 9001 updated certification as well as our certification for ISO 13485, which replaced our EN 46001 certification.

Employees

As of December 31, 2007, we had 295 employees, including 134 employees in sales and marketing functions, 29 employees in research, development and engineering functions, 98 employees in manufacturing and service functions and 34 employees in general and administrative functions. We believe that our future success will depend in part on our continued ability to attract, hire and retain qualified personnel. None of our employees is represented by a labor union, and we believe our employee relations are good.

ITEM 1A. ***Risk Factors.***

The following important factors, among others, could cause our actual operating results to differ materially from those indicated or suggested by forward-looking statements made in this Annual Report or presented elsewhere by management from time to time.

Risks Related to Our Business and Industry

We have a history of operating losses, and we may not maintain profitability.

Although we were profitable in 2004, 2005 and 2007, we incurred operating losses in two of the last five years. Our net losses were approximately $0.7 million in 2006 and $0.5 million in 2003. We may not be able to sustain or increase profitability on a quarterly or annual basis. If we are unable to maintain profitability, the market value of our stock will decline, and you could lose all or a part of your investment.

Our competition may prevent us from achieving further market penetration or improving operating results.

Competition in the aesthetic laser industry is intense. Our products compete against products offered by public companies, such as Candela Corporation, Cutera, Inc., Laserscope, Lumenis Ltd., Palomar Medical Technologies, Inc., Syneron Medical Ltd. and Thermage, Inc., as well as several smaller specialized private companies, such as Reliant Technology, Inc. and Alma Lasers, Ltd. Some of these competitors have greater financial and human resources than we do and have established reputations, as well as worldwide distribution channels and sales and marketing capabilities that are larger and more established than ours. Additional competitors may enter the market, and we are likely to compete with new companies in the future.

We also face competition from medical products, such as BOTOX(R) and collagen injections, and surgical and non-surgical aesthetic procedures, such as face lifts, sclerotherapy, electrolysis, microdermabrasion and chemical peels. We may also face competition from manufacturers of pharmaceutical and other products that have not yet been developed. As a result of competition with these companies, products and procedures, we could experience loss of market share and decreasing revenue as well as reduced prices and profit margins, any of which would harm our business and operating results.

Our ability to compete effectively depends upon our ability to distinguish our company and our products from our competitors and their products. Factors affecting our competitive position include:

- product performance and design;
- ability to sell products tailored to meet the applications needs of clients and patients;
- quality of customer support;
- product pricing;
- product safety;
- sales, marketing and distribution capabilities;
- success and timing of new product development and introductions; and
- intellectual property protection.

If we fail to obtain Alexandrite rods or our air cooling system from our sole suppliers, our ability to manufacture and sell our products and components would be impaired.

We use Alexandrite rods to manufacture the lasers for our *Apogee* products. We depend exclusively on Northrop Grumman SYNOPTICS to supply Alexandrite rods to us, and we are aware of no alternative supplier meeting our quality standards. We offer our *SmartCool*(R) treatment cooling systems for use with our laser aesthetic treatment systems, and we depend exclusively on Zimmer Elektromedizin GmbH to supply *SmartCool* systems to us. Both Alexandrite lasers and our *SmartCool* systems are important to our business.

We do not have long-term arrangements with Northrop Grumman SYNOPTICS or Zimmer Elektromedizin for the supply of Alexandrite rods or *SmartCool* systems, but instead purchase from them on a purchase order basis. Northrop Grumman SYNOPTICS and Zimmer Elektromedizin are not required, and may not be able or willing, to meet our future requirements at current prices, or at all. Any extended interruption in our supplies of Alexandrite rods or our *SmartCool* treatment cooling systems could materially harm our business.

If we do not continue to develop and commercialize new products and identify new markets for our products and technology, we may not remain competitive, and our revenues and operating results could suffer.

The aesthetic laser and light-based treatment system industry is subject to continuous technological development and product innovation. If we do not continue to be innovative in the development of new products and applications, our competitive position will likely deteriorate as other companies successfully design and commercialize new products and applications. Accordingly, our success depends in part on developing new and innovative applications of laser and other light-based technology and identifying new markets for and applications of existing products and technology. If we are unable to develop and commercialize new products and identify new markets for our products and technology, our products and technology could become obsolete and our revenues and operating results could be adversely affected.

To remain competitive, we must:

- develop or acquire new technologies that either add to or significantly improve our current products;
- convince our target customers that our new products or product upgrades would be attractive revenue-generating additions to their practices;
- sell our products to non-traditional customers, including primary care physicians, gynecologists and other specialists;
- identify new markets and emerging technological trends in our target markets and react effectively to technological changes; and
- maintain effective sales and marketing strategies.

If our new products do not gain market acceptance, our revenues and operating results could suffer.

The commercial success of the products and technology we develop will depend upon the acceptance of these products by providers of aesthetic procedures and their patients and clients. It is difficult for us to predict how successful recently introduced products, or products we are currently developing, will be over the long term. If the products we develop do not gain market acceptance, our revenues and operating results could suffer.

We expect that many of the products we develop will be based upon new technologies or new applications of existing technologies. It may be difficult for us to achieve market acceptance of some of our products, particularly the first products that we introduce to the market based on new technologies or new applications of existing technologies.

If demand for our aesthetic treatment systems by non-traditional physician customers and spas does not develop as we expect, our revenues will suffer and our business will be harmed.

Our revenues from non-traditional physician customers and spa purchasers of our products have increased significantly since January 1, 2004. We believe, and our growth expectations assume, that we and other companies selling lasers and other light-based aesthetic treatment systems have only begun to penetrate these markets and that our revenues from selling to these markets will continue to increase. If our expectations as to the size of these markets and our ability to sell our products to participants in these markets are not correct, our revenues will suffer and our business will be harmed.

We rely upon third party suppliers for the components and subassemblies of many of our products, making us vulnerable to supply shortages and price fluctuations, which could harm our business.

Many of the components and subassemblies that comprise our aesthetic treatment systems are currently manufactured for us by a limited number of suppliers. In addition, one third party supplier assembles and tests many of the components and subassemblies for our *Apogee, Cynergy, Affirm, Acclaim* and *VStar* product families. We do not have long-term contracts with any of these third parties, including the third party supplier that assembles many of our components and subassemblies, for the supply of parts or services. Any interruption in the supply of components or subassemblies, or our inability to obtain substitute components or subassemblies from alternate sources at acceptable prices in a timely manner, or our inability to obtain assembly and testing services, could impair our ability to meet the demand of our customers, which would have an adverse effect on our business and operating results.

We sell our products in numerous international markets. Our operating results may suffer if we are unable to manage our international operations effectively.

We sell our products in 50 foreign countries, and we therefore are subject to risks associated with having international operations. Sales of our products outside of North America accounted for 36% of our revenue for 2007, 42% of our revenue for 2006 and 41% of our revenue in 2005.

Our international sales are subject to a number of risks, including:

- foreign certification and regulatory requirements;
- difficulties in staffing and managing our foreign operations;
- import and export controls; and
- political and economic instability.

Revenue from our international sales could be adversely affected by fluctuations in currency exchange rates, which would cause our operating results to suffer.

We face risks associated with changes in foreign currency exchange rates. Revenues outside of North America that were recorded in U.S. dollars represented approximately 46% of our total 2007 revenues outside of North America. Substantially all of the remaining 54% of our total 2007 revenues outside of North America were sales in euros, British pounds and Japanese yen. Since we report our financial position and results of operations in U.S. dollars, our reported results of operations may be adversely affected by changes in the exchange rate between these currencies and the U.S. dollar. We have not historically engaged in hedging activities relating to our non-U.S. dollar operations. We may incur negative foreign currency translation charges as a result of changes in currency exchange rates, which could cause our operating results to suffer.

We rely on third party distributors to market, sell and service a significant portion of our products. If these distributors do not commit the necessary resources to effectively market, sell and service our products or if our relationships with these distributors are disrupted, our business and operating results may be harmed.

In North America, the United Kingdom, Germany, Spain, France, Japan and China, we sell our products through our internal sales organization. Outside of these markets, we sell our products through third party distributors. Our sales and marketing success in these other markets depends on these distributors, in particular their sales and service expertise and relationships with the customers in the marketplace. Sales of our aesthetic treatment systems by third party distributors represented 17% of our product revenue in 2007, 18% of our product revenue in 2006 and 17% of our product revenue in 2005. We do not control these distributors, and they may not be successful in marketing our products. Third party distributors may terminate their relationships with us, or fail to commit the necessary resources to market and sell our products to the level of our expectations. Currently, we have written distributor agreements in place with 18 of our 19 third party distributors. The third party distributors with which we do not have written distributor agreements may terminate their relationships with us and stop selling and servicing our products with little or no notice. If current or future third party distributors do not perform adequately, or if we fail to maintain our existing relationships with these distributors or fail to recruit and retain distributors in particular geographic areas, our revenue from international sales may be adversely affected and our operating results could suffer.

Because we do not require training for users of our non-invasive products, and sell these products to non-physicians, there exists an increased potential for misuse of these products, which could harm our reputation and our business.

Federal regulations allow us to sell our products to or on the order of practitioners licensed by law to use or order the use of a prescription device. The definition of "licensed practitioners" varies from state to state. As a result, our products may be purchased or operated by physicians with varying levels of training and, in many states, by non-physicians, including nurse practitioners, chiropractors and technicians. Outside the United States, many jurisdictions do not require specific qualifications or training for purchasers or operators of our products. We do not supervise the procedures performed with our non-invasive products, nor do we require that direct medical supervision occur. We and our distributors offer product training sessions, but neither we nor our distributors require purchasers or operators of our non-invasive products to attend training sessions. The lack of required training and the purchase and use of our non-invasive products by non-physicians may result in product misuse and adverse treatment outcomes, which could harm our reputation and expose us to costly product liability litigation.

Product liability suits could be brought against us due to a defective design, material or workmanship or due to misuse of our products. These lawsuits could be expensive and time consuming and result in substantial damages to us and increases in our insurance rates.

If our products are defectively designed, manufactured or labeled, contain defective components or are misused, we may become subject to substantial and costly litigation by our customers or their patients or clients. Misusing our products or failing to adhere to operating guidelines for our products can cause severe burns or other damage to the eyes, skin or other tissue. We are routinely involved in claims related to the use of our products. Product liability claims could divert management's attention from our core business, be expensive to defend and result in sizable damage awards against us. Our current insurance coverage may not be sufficient to cover these claims. Moreover, in the future, we may not be able to obtain insurance in amount or scope sufficient to provide us with adequate coverage against potential liabilities. Any product liability claims brought against us, with or without merit, could increase our product liability insurance rates or prevent us from securing continuing coverage, could harm our reputation in the industry and reduce product sales. We would need to pay any product losses in excess of our insurance coverage out of cash reserves, harming our financial condition and adversely affecting our operating results.

We may incur substantial expenses if our past practices are shown to have violated the Telephone Consumer Protection Act.

We previously used facsimiles to disseminate information about our clinical workshops to large numbers of customers and potential customers. These facsimiles were transmitted by third parties retained by us, and were sent to recipients whose facsimile numbers were supplied by us as well as other recipients whose facsimile numbers we purchased from other sources. In May 2005, we stopped sending unsolicited facsimiles to customers and potential customers.

Under the federal Telephone Consumer Protection Act, or TCPA, recipients of unsolicited facsimile "advertisements" are entitled to damages of up to $500 per facsimile for inadvertent violations and up to $1,500 per facsimile for knowing or willful violations. Recipients of unsolicited facsimile advertisements may seek enforcement of the TCPA in state courts. The TCPA also permits states to initiate a civil action in a federal district court to enforce the TCPA against a party who engages in a pattern or practice of violations of the TCPA. In addition, complaints may be filed with the Federal Communications Commission, which has the power to assess penalties against parties for violations of the TCPA.

In May 2005, we were sued in Massachusetts state court by Dr. Ari Weitzner, individually and as putative representative of a purported class under the TCPA. The lawsuit alleges that we violated the TCPA by sending unsolicited advertisements by facsimile. We believe the number of unsolicited facsimiles to be quite large.

We are vigorously defending the Weitzner lawsuit, but litigation is subject to numerous uncertainties and we are unable to predict the ultimate outcome of this matter. Even if we prevail in this lawsuit, other individual or class action claims may be brought against us alleging past violations of the TCPA. Moreover, the amount of any potential liability in connection with this lawsuit or other possible lawsuits will depend, to a large extent, on whether a class in a class action lawsuit is certified and, if one is certified, on the scope of the class, neither of which we can predict at this time.

We have not recorded a liability related to this lawsuit or other possible future lawsuits. However, we may determine in the future that an accrual is required, and we may be required to pay damages in respect of this lawsuit or other possible future lawsuits arising out of our past transmission of facsimiles, any of which could materially and adversely affect our results of operations, cash flows and financial condition. Regardless of the outcome, this lawsuit or other possible future lawsuits may cause us to incur significant expenses and divert the attention of our management and key personnel from our business operations.

We have tendered a claim with respect to the Weitzner lawsuit to our general liability insurance carrier and coverage has been disputed. Although the carrier has previously provided coverage for several small individual claims brought against us under the TCPA, the carrier has denied coverage for this claim. Even if coverage is determined to apply, since the potential liability under this claim and other possible future claims could be substantial, our coverage may not be sufficient to satisfy any damages that we may be required to pay.

Our financial results may fluctuate from quarter to quarter, which makes our results difficult to predict and could cause our results to fall short of expectations.

Our financial results may fluctuate as a result of a number of factors, many of which are outside of our control. For these reasons, comparing our financial results on a period-to-period basis may not be meaningful, and you should not rely on our past results as an indication of our future performance. Our future quarterly and annual expenses as a percentage of our revenues may be significantly different from those we have recorded in the past or which we expect for the future. Our financial results in some quarters may fall below our expectations

or the expectations of market analysts or investors. Any of these events could cause our stock price to fall. Each of the risk factors listed in this "Risk Factors" section, and the following factors, may adversely affect our financial results:

- continued availability of attractive equipment leasing terms for our customers, which may be negatively influenced by interest rate increases;
- increases in the length of our sales cycle; and
- reductions in the efficiency of our manufacturing processes.

If there is not sufficient demand for the procedures performed with our products, practitioner demand for our products could decline, which would adversely affect our operating results.

Most procedures performed using our aesthetic treatment systems are elective procedures that are not reimbursable through government or private health insurance. The cost of these elective procedures must be borne by the patient. As a result, the decision to undergo a procedure that utilizes our products may be influenced by a number of factors, including:

- patient awareness of procedures and treatments;
- the cost, safety and effectiveness of the procedure and of alternative treatments;
- the success of our and our customers' sales and marketing efforts to purchasers of these procedures; and
- consumer confidence, which may be affected by economic and other conditions.

If there is not sufficient demand for the procedures performed with our products, practitioner demand for our products would be reduced, which would adversely affect our operating results.

Our business and operations are experiencing rapid growth. If we fail to effectively manage our growth, our business and operating results could be harmed.

We have experienced significant growth in the scope of our operations and the number of our employees. For example, our revenue increased from $27.1 million in 2003 to $124.3 million in 2007, and the number of our employees increased from 138 at the beginning of 2003 to 295 as of December 31, 2007. This growth has placed significant demands on our management, as well as our financial and operational resources. If we do not effectively manage our growth, the efficiency of our operations and the quality of our products could suffer, which could adversely affect our business and operating results. To effectively manage this growth, we will need to continue to:

- implement appropriate operational, financial and management controls, systems and procedures;
- expand our manufacturing capacity and scale of production;
- expand our sales, marketing and distribution infrastructure and capabilities; and
- provide adequate training and supervision to maintain high quality standards.

We may be unable to attract and retain management and other personnel we need to succeed.

Our success depends on the services of our senior management and other key research and development, manufacturing, sales and marketing employees. The loss of the services of one or more of these employees could have a material adverse effect on our business. We consider retaining Michael R. Davin, our president and chief executive officer, to be key to our efforts to develop, sell and market our products and remain competitive. We have entered into an employment agreement with Mr. Davin; however, the employment agreement is terminable

by him on short notice and may not ensure his continued service with our company. Our future success will depend in large part upon our ability to attract, retain and motivate highly skilled employees. We cannot be certain that we will be able to do so.

Any acquisitions that we make could disrupt our business and harm our financial condition.

From time to time, we evaluate potential strategic acquisitions of complementary businesses, products or technologies, as well as consider joint ventures and other collaborative projects. We may not be able to identify appropriate acquisition candidates or strategic partners, or successfully negotiate, finance or integrate any businesses, products or technologies that we acquire. We do not have any experience with acquiring companies or products. Any acquisition we pursue could diminish our cash available to us for other uses or be dilutive to our stockholders, and could divert management's time and resources from our core operations.

El.En. has substantial control over us. In addition, El.En. and our executive officers and directors have the ability to control all matters submitted to stockholders for approval.

In addition to the factors discussed below regarding El.En.'s ability to control the election of a majority of the members of our board of directors, El.En. and our executive officers and directors, in the aggregate, beneficially own approximately 24% of our outstanding common stock. As a result, if these stockholders were to act together, they would be able to control all matters submitted to our stockholders for approval. For example, these persons could control any amendment of our certificate of incorporation and bylaws and approval of any merger, consolidation or sale of all or substantially all of our assets. This concentration of voting power could delay or prevent an acquisition of our company on terms that other stockholders may desire. Please also see the discussion under "Risks Related to Our Relationship with El.En.—El.En. has substantial control over us and could delay or prevent a change of control."

Provisions in our corporate charter documents and under Delaware law may delay or prevent attempts by our stockholders to change our management and hinder efforts to acquire a controlling interest in us.

Provisions of our certificate of incorporation and bylaws may discourage, delay or prevent a merger, acquisition or other change in control that stockholders may consider favorable, including transactions in which you might otherwise receive a premium for your shares. These provisions may also prevent or frustrate attempts by our stockholders to replace or remove our management. These provisions include:

- a dual class capital structure that allows El.En. to control the election of a majority of the members of our board of directors;
- the classification of the members of our directors who are elected by holders of our class A common stock and class B common stock, voting together as a single class;
- limitations on the removal of directors who are elected by holders of our class A common stock and class B common stock, voting together as a single class;
- advance notice requirements for stockholder proposals and nominations;
- the inability of class A stockholders to act by written consent or to call special meetings; and
- the ability of our board of directors to designate the terms of and issue new series of preferred stock without stockholder approval, which could be used to institute a "poison pill" that would work to dilute the stock ownership of a potential hostile acquirer, effectively preventing acquisitions that have not been approved by our board of directors.

The affirmative vote of the holders of at least 75% of our shares of capital stock entitled to vote is necessary to amend or repeal the above provisions of our certificate of incorporation, and the right of the holders of shares of our class B common stock to elect a majority of the members of our board of directors may not be modified

without the approval of the holders of at least a majority of the shares of our class B common stock outstanding. In addition, absent approval of our board of directors, our bylaws may only be amended or repealed by the affirmative vote of the holders of at least 75% of the voting power of our shares of capital stock entitled to vote and the affirmative vote of holders of at least a majority of the shares of class B common stock outstanding.

In addition, Section 203 of the Delaware General Corporation Law prohibits a publicly held Delaware corporation from engaging in a business combination with an interested stockholder, generally a person which together with its affiliates owns or within the last three years has owned 15% of our voting stock, for a period of three years after the date of the transaction in which the person became an interested stockholder, unless the business combination is approved in a prescribed manner. Accordingly, Section 203 may discourage, delay or prevent a change in control of our company.

Our stock price may be volatile.

Our class A common stock price may be volatile. The stock market in general has experienced extreme volatility that has often been unrelated to the operating performance of particular companies. The market price for our class A common stock may be influenced by many factors, including:

- the success of competitive products or technologies;
- regulatory developments in the United States and foreign countries;
- developments or disputes concerning patents or other proprietary rights;
- the recruitment or departure of key personnel;
- variations in our financial results or those of companies that are perceived to be similar to us;
- market conditions in the our industry and issuance of new or changed securities analysts' reports or recommendations; and
- general economic, industry and market conditions.

A significant portion of our total outstanding shares are restricted from immediate resale but may be sold into the market in the near future. This could cause the market price of our class A common stock to drop significantly, even if our business is doing well.

Sales of a substantial number of shares of our class A common stock, including shares of our class B common stock that have been converted into shares of our class A common stock, in the public market could occur at any time. These sales, or the perception in the market that the holders of a large number of shares intend to sell shares, could reduce the market price of our class A common stock. We also intend to register all shares of our class A common stock that we may issue under our employee benefit plans.

Due to our current inability to sell certain of our Auction Rate Securities, the securities may experience an other-than-temporary decline in value, and funds associated with the securities may be inaccessible in excess of 12 months, resulting in an adverse impact to our income and results of operations.

Our marketable securities portfolio, which totaled $47.1 million at December 31, 2007, included Auction Rate Securities, or ARS, of $29.3 million from various issuers collateralized by student loans and municipal debt. ARSs are securities with long-term contractual maturities but with interest rates that are reset every seven to 35 days by auctions. At the end of each reset period, investors can sell or continue to hold the securities at par. On February 13, 2008, certain ARSs that we hold experienced failed auctions that limited the liquidity of these securities. Based on current market conditions, it is likely that auction failures will continue and could result in either temporary or other-than-temporary impairments of our ARS holdings. We have the ability and intent to hold these securities until a successful auction occurs and the ARSs are liquidated at par value. If in the future we

determine that any decline in value of the ARSs is other-than-temporary, we would be required to recognize the loss in our statement of operations, which could have a material impact on our operating results in the period it is recognized. Further, as the funds associated with the ARSs may not be accessible for longer than twelve months because of continued failed auctions or our inability to find a buyer outside of the auction process, we may classify these securities as long-term assets in our consolidated balance sheet as of March 31, 2008, or thereafter.

Risks Related to Our Relationship with El.En.

El.En. has substantial control over us and could delay or prevent a change of control.

El.En., our largest stockholder, is able to control the election of a majority of the members of our board of directors. El.En. owns approximately 100% of our outstanding class B common stock, which comprises 24% of our aggregate outstanding common. Until El.En. beneficially owns less than 20% of the aggregate number of shares of our class A common stock and class B common stock outstanding or less than 50% of the number of shares of our class B common stock outstanding, El.En., as holder of a majority of the shares of our class B common stock, will have the right:

- to elect a majority of the members of our board of directors;
- to approve amendments to our bylaws adopted by our class A and class B stockholders, voting as a single class; and
- to approve amendments to any provisions of our restated certificate of incorporation relating to the rights of holders of common stock, the powers, election and classification of the board of directors, corporate opportunities and the rights of holders of class A common stock and class B common stock to elect and remove directors, act by written consent and call special meetings of stockholders.

In addition, the holders of shares of our class B common stock will vote with our class A stockholders for the election of the remaining directors.

Because El.En. is the holder of a majority of the shares of our class B common stock, El.En.'s approval will be required for any of the actions described above. In addition, because El.En. will be able to control the election of a majority of our board, and because of its substantial holdings of our capital stock, El.En. will likely have the ability to delay or prevent a change of control of our company that may be favored by other directors or stockholders and otherwise exercise substantial control over all corporate actions requiring board or stockholder approval.

El.En. and its subsidiaries market and sell products that compete with our products, and any competition by El.En. could have a material adverse effect on our business.

El.En. is a leading laser manufacturer in Europe and a leading light-based medical device manufacturer worldwide. El.En. and its subsidiaries develop and produce laser systems with scientific, industrial, commercial and medical applications. Although we have exclusive North American distribution rights for our *TriActive LaserDermology* and *Smartlipo* products, El.En. may compete with us in North America with its other products. In the event that our distribution agreements with El.En. terminate, El.En. may compete with us in North America with these products. El.En. markets, sells, promotes and licenses products that compete with our products outside of North America. Our business could be materially and adversely affected by competition from El.En.

Conflicts of interest may arise between us and El.En., and these conflicts might ultimately be resolved in a manner unfavorable to us.

For financial reporting purposes, our financial results are included in El.En.'s consolidated financial statements. One of our directors, Andrea Cangioli, and the spouse of one of our directors, Leonardo Masotti, are

also officers or directors of El.En. These two directors own or have an interest in substantial amounts of El.En. stock. Ownership interests of our directors in El.En. stock, or service as a director of our company while at the same time serving as, or being the spouse of, a director or officer of El.En., could give rise to conflicts of interest when a director or officer is faced with a decision that could have different implications for the two companies.

Conflicts may arise with respect to possible future distribution and research and development arrangements with El.En. or another El.En. affiliated company in which the terms and conditions of the arrangements are subject to negotiation between us and El.En. or such other El.En. affiliated company. These potential conflicts could also arise, for example, over matters such as:

- the nature, timing, marketing, distribution and price of our products and El.En.'s products that compete with each other;
- intellectual property matters; and
- business opportunities that may be attractive to both El.En. and us.

In order to address potential conflicts of interest between us and El.En., our restated certificate of incorporation contains provisions regulating and defining the conduct of our affairs as they may involve El.En. and El.En. affiliated companies and El.En.'s officers and directors who serve as our directors. These provisions recognize that we and El.En. and El.En. affiliated companies engage and may continue to engage in the same or similar business activities and lines of business and will continue to have contractual and business relations with each other. These provisions expressly permit El.En. and its affiliated companies to compete against us and narrowly limit corporate opportunities that El.En. or its directors or officers who serve as our directors must make available to us.

Our class A share price may decline because of future sales of our shares by El.En.

El.En. may sell all or part of the shares of our class B common stock that it owns, at which time those shares would automatically convert into shares of our class A common stock. El.En. is not subject to any contractual obligation to maintain its ownership position in our shares. Consequently, El.En. may not maintain its ownership of our common stock. Sales by El.En. of substantial amounts of our common stock in the public market could adversely affect prevailing market prices for our class A common stock.

If El.En. sells the shares of our stock held by it and no longer has control over us, our commercial relationship with El.En. may be adversely affected.

El.En. has advised us that it currently does not intend to sell its shares of our common stock in the foreseeable future. However, El.En.'s plans and intentions may change at any time. El.En. is not subject to any contractual obligation to maintain an ownership position in our shares.

If El.En. sells our shares and no longer has control over us, El.En. will cease to include our financial results in its consolidated financial statements, and El.En.'s interests may differ significantly from ours. If this occurs, our commercial relationship with El.En. may be adversely affected, which, in turn, could have a material adverse effect on our business. For example, if El.En. does not have a continuing interest in our financial success, it may be more inclined to compete with us in North America and in other markets, not to enter into future commercial agreements with us or to terminate or not renew our existing distribution agreements. If any of these events were to occur, it could harm our business.

Risks Related to Intellectual Property

If we infringe or are alleged to infringe intellectual property rights of third parties, our business could be adversely affected.

Our products may infringe or be claimed to infringe patents or patent applications under which we do not hold licenses or other rights. Third parties may own or control these patents and patent applications in the United States and abroad. These third parties could bring claims against us that would cause us to incur substantial expenses and, if successfully asserted against us, could cause us to pay substantial damages. Further, if a patent infringement suit were brought against us, we could be forced to stop or delay manufacturing or sales of the product that is the subject of the suit.

As a result of patent infringement claims, or in order to avoid potential claims, we may choose or be required to seek a license from the third party and be required to pay license fees or royalties or both. These licenses may not be available on acceptable terms, or at all. Even if we were able to obtain a license, the rights may be nonexclusive, which could result in our competitors gaining access to the same intellectual property. Ultimately, we could be forced to cease some aspect of our business operations if, as a result of actual or threatened patent infringement claims, we are unable to enter into licenses on acceptable terms. This could harm our business significantly.

There has been substantial litigation and other proceedings regarding patent and other intellectual property rights in our industry. In addition to infringement claims against us, we may become a party to other types of patent litigation and other proceedings, including interference proceedings declared by the United States Patent and Trademark Office and opposition proceedings in the European Patent Office, regarding intellectual property rights with respect to our products and technology. The cost to us of any patent litigation or other proceeding, even if resolved in our favor, could be substantial. Some of our competitors may be able to sustain the costs of such litigation or proceedings more effectively than we can because of their greater financial resources. Uncertainties resulting from the initiation and continuation of patent litigation or other proceedings could have a material adverse effect on our ability to compete in the marketplace. Patent litigation and other proceedings may also absorb significant management time.

If we are unable to obtain or maintain intellectual property rights relating to our technology and products, the commercial value of our technology and products will be adversely affected and our competitive position could be harmed.

Our success and ability to compete depends in part upon our ability to obtain protection in the United States and other countries for our products by establishing and maintaining intellectual property rights relating to or incorporated into our technology and products. We own a variety of patents and patent applications in the United States and corresponding patents and patent applications in many foreign jurisdictions. To date, however, our patent estate has not stopped other companies from competing against us, and we do not know how successful we would be should we choose to assert our patents against suspected infringers. Our pending and future patent applications may not issue as patents or, if issued, may not issue in a form that will be advantageous to us. Even if issued, patents may be challenged, narrowed, invalidated or circumvented, which could limit our ability to stop competitors from marketing similar products or limit the length of term of patent protection we may have for our products. Changes in either patent laws or in interpretations of patent laws in the United States and other countries may diminish the value of our intellectual property or narrow the scope of our patent protection.

If we are unable to protect the confidentiality of our proprietary information and know-how, the value of our technology and products could be adversely affected.

In addition to patented technology, we rely upon unpatented proprietary technology, processes and know-how, particularly with respect to our Alexandrite and pulse dye lasers. We generally seek to protect this information in part by confidentiality agreements with our employees, consultants and third parties. These

agreements may be breached, and we may not have adequate remedies for any such breach. In addition, our trade secrets may otherwise become known or be independently developed by competitors.

Risks Related to Government Regulation

If we fail to obtain and maintain necessary U.S. Food and Drug Administration clearances for our products and indications or if clearances for future products and indications are delayed or not issued, our business would be harmed.

Our products are classified as medical devices and are subject to extensive regulation by the FDA and other federal, state and local authorities. These regulations relate to manufacturing, labeling, sale, promotion, distribution, importing and exporting and shipping of our products. In the United States, before we can market a new medical device, or a new use of, or claim for, an existing product, we must first receive either 510(k) clearance or premarket approval from the FDA, unless an exemption applies. Both of these processes can be expensive and lengthy and entail significant user fees, unless exempt. The FDA's 510(k) clearance process usually takes from three to 12 months, but it can last longer. The process of obtaining premarket approval is much more costly and uncertain than the 510(k) clearance process. It generally takes from one to three years, or even longer, from the time the premarket approval application is submitted to the FDA until an approval is obtained.

In order to obtain premarket approval and, in some cases, a 510(k) clearance, a product sponsor must conduct well controlled clinical trials designed to test the safety and effectiveness of the product. Conducting clinical trials generally entails a long, expensive and uncertain process that is subject to delays and failure at any stage. The data obtained from clinical trials may be inadequate to support approval or clearance of a submission. In addition, the occurrence of unexpected findings in connection with clinical trials may prevent or delay obtaining approval or clearance. If we conduct clinical trials, they may be delayed or halted, or be inadequate to support approval or clearance, for numerous reasons, including:

- FDA, other regulatory authorities or an institutional review board may place a clinical trial on hold;
- patients may not enroll in clinical trials, or patient follow-up may not occur, at the rate we expect;
- patients may not comply with trial protocols;
- institutional review boards and third party clinical investigators may delay or reject our trial protocol;
- third party clinical investigators may decline to participate in a trial or may not perform a trial on our anticipated schedule or consistent with the clinical trial protocol, good clinical practices, or other FDA requirements;
- third party organizations may not perform data collection and analysis in a timely or accurate manner;
- regulatory inspections of our clinical trials or manufacturing facilities may, among other things, require us to undertake corrective action or suspend or terminate our clinical trials, or invalidate our clinical trials;
- changes in governmental regulations or administrative actions; and
- the interim or final results of the clinical trials may be inconclusive or unfavorable as to safety or effectiveness.

Medical devices may be marketed only for the indications for which they are approved or cleared. The FDA may not approve or clear indications that are necessary or desirable for successful commercialization. Indeed, the FDA may refuse our requests for 510(k) clearance or premarket approval of new products, new intended uses or modifications to existing products. Our clearances can be revoked if safety or effectiveness problems develop.

After clearance or approval of our products, we are subject to continuing regulation by the FDA, and if we fail to comply with FDA regulations, our business could suffer.

Even after clearance or approval of a product, we are subject to continuing regulation by the FDA, including the requirements that our facility be registered and our devices listed with the agency. We are subject to Medical Device Reporting regulations, which require us to report to the FDA if our products may have caused or contributed to a death or serious injury or malfunction in a way that would likely cause or contribute to a death or serious injury if the malfunction were to recur. We must report corrections and removals to the FDA where the correction or removal was initiated to reduce a risk to health posed by the device or to remedy a violation of the Federal Food, Drug, and Cosmetic Act caused by the device that may present a risk to health, and maintain records of other corrections or removals. The FDA closely regulates promotion and advertising and our promotional and advertising activities could come under scrutiny. Since 1994, we have received five untitled letters from the FDA regarding alleged violations caused by our promotional activities. We have responded to these letters and the FDA has found our responses acceptable. If the FDA objects to our promotional and advertising activities or finds that we failed to submit reports under the Medical Device Reporting regulations, for example, the FDA may allege our activities resulted in violations.

The FDA and state authorities have broad enforcement powers. Our failure to comply with applicable regulatory requirements could result in enforcement action by the FDA or state agencies, which may include any of the following sanctions:

- untitled letters, warning letters, fines, injunctions, consent decrees and civil penalties;
- repair, replacement, refunds, recall or seizure of our products;
- operating restrictions or partial suspension or total shutdown of production;
- refusing or delaying our requests for 510(k) clearance or premarket approval of new products or new intended uses;
- withdrawing 510(k) clearance or premarket approvals that have already been granted; and
- criminal prosecution.

If any of these events were to occur, they could harm our business.

Federal regulatory reforms may adversely affect our ability to sell our products profitably.

From time to time, legislation is drafted and introduced in Congress that could significantly change the statutory provisions governing the clearance or approval, manufacture and marketing of a device. In addition, FDA regulations and guidance are often revised or reinterpreted by the agency in ways that may significantly affect our business and our products. It is impossible to predict whether legislative changes will be enacted or FDA regulations, guidance or interpretations changed, and what the impact of such changes, if any, may be.

We have modified some of our products without FDA clearance. The FDA could retroactively determine that the modifications were improper and require us to stop marketing and recall the modified products.

Any modifications to one of our FDA-cleared devices that could significantly affect its safety or effectiveness, or that would constitute a major change in its intended use, requires a new 510(k) clearance or a premarket approval. We may be required to submit extensive pre-clinical and clinical data depending on the nature of the changes. We may not be able to obtain additional 510(k) clearances or premarket approvals for modifications to, or additional indications for, our existing products in a timely fashion, or at all. Delays in obtaining future clearances or approvals would adversely affect our ability to introduce new or enhanced products in a timely manner, which in turn would harm our revenue and operating results. We have made modifications to our devices in the past and may make additional modifications in the future that we believe do

not or will not require additional clearances or approvals. If the FDA disagrees, and requires new clearances or approvals for the modifications, we may be required to recall and to stop marketing the modified devices, which could harm our operating results and require us to redesign our products.

If we fail to comply with the FDA's Quality System Regulation and laser performance standards, our manufacturing operations could be halted, and our business would suffer.

We are currently required to demonstrate and maintain compliance with the FDA's QSR. The QSR is a complex regulatory scheme that covers the methods and documentation of the design, testing, control, manufacturing, labeling, quality assurance, packaging, storage and shipping of our products. Because our products involve the use of lasers, our products also are covered by a performance standard for lasers set forth in FDA regulations. The laser performance standard imposes specific record keeping, reporting, product testing and product labeling requirements. These requirements include affixing warning labels to laser products as well as incorporating certain safety features in the design of laser products. The FDA enforces the QSR and laser performance standards through periodic unannounced inspections. We have been, and anticipate in the future being, subject to such inspections. Our failure to comply with the QSR or to take satisfactory corrective action in response to an adverse QSR inspection or our failure to comply with applicable laser performance standards could result in enforcement actions, including a public warning letter, a shutdown of or restrictions on our manufacturing operations, delays in approving or clearing a product, refusal to permit the import or export of our products, a recall or seizure of our products, fines, injunctions, civil or criminal penalties, or other sanctions, such as those described in the preceding paragraphs, any of which could cause our business and operating results to suffer.

If we fail to comply with state laws and regulations, or if state laws or regulations change, our business could suffer.

In addition to FDA regulations, most of our products are also subject to state regulations relating to their sale and use. These regulations are complex and vary from state to state, which complicates monitoring compliance. In addition, these regulations are in many instances in flux. For example, federal regulations allow our prescription products to be sold to or on the order of "licensed practitioners," that is, practitioners licensed by law to use or order the use of a prescription device. Licensed practitioners are defined on a state-by-state basis. As a result, some states permit non-physicians to purchase and operate our products, while other states do not. Additionally, a state could change its regulations at any time to prohibit sales to particular types of customers. We believe that, to date, we have sold our prescription products only to licensed practitioners. However, our failure to comply with state laws or regulations and changes in state laws or regulations may adversely affect our business.

We or our distributors may be unable to obtain or maintain international regulatory qualifications or approvals for our current or future products and indications, which could harm our business.

Sales of our products outside the United States are subject to foreign regulatory requirements that vary widely from country to country. In many countries, our third party distributors are responsible for obtaining and maintaining regulatory approvals for our products. We do not control our third party distributors, and they may not be successful in obtaining or maintaining these regulatory approvals. In addition, the FDA regulates exports of medical devices from the United States.

Complying with international regulatory requirements can be an expensive and time consuming process, and approval is not certain. The time required to obtain foreign clearances or approvals may be longer than that required for FDA clearance or approval, and requirements for such clearances or approvals may differ significantly from FDA requirements. Foreign regulatory authorities may not clear or approve our products for the same indications cleared or approved by the FDA. The foreign regulatory approval process may include all of the risks associated with obtaining FDA clearance or approval in addition to other risks. Although we or our

distributors have obtained regulatory approvals in the European Union and other countries outside the United States for many of our products, we or our distributors may be unable to maintain regulatory qualifications, clearances or approvals in these countries or obtain qualifications, clearances or approvals in other countries. For example, we are in the process of seeking regulatory approvals from the Japanese Ministry of Health, Labour and Welfare for the direct sale of our products into that country. If we are not successful in doing so, our business will be harmed. We may also incur significant costs in attempting to obtain and in maintaining foreign regulatory clearances, approvals or qualifications.

Foreign regulatory agencies, as well as the FDA, periodically inspect manufacturing facilities both in the United States and abroad. If we experience delays in receiving necessary qualifications, clearances or approvals to market our products outside the United States, or if we fail to receive those qualifications, clearances or approvals, or if we fail to comply with other foreign regulatory requirements, we and our distributors may be unable to market our products or enhancements in international markets effectively, or at all. Additionally, the imposition of new requirements may significantly affect our business and our products. We may not be able to adjust to such new requirements.

New regulations may limit our ability to sell to non-physicians, which could harm our business.

Currently, we sell our products primarily to physicians and, outside the United States, to aestheticians. In addition, we recently began marketing our products to the growing aesthetic spa market, where non-physicians under physician supervision perform aesthetic procedures at dedicated facilities. However, federal, state and international regulations could change at any time, disallowing sales of our products to aestheticians, and limiting the ability of aestheticians and non-physicians to operate our products. Any limitations on our ability to sell our products to non-physicians or on the ability of aestheticians and non-physicians to operate our products could cause our business and operating results to suffer.

Item 1B. *Unresolved Staff Comments*

None.

Item 2. *Properties*

In July 2005, we moved our executive offices and our manufacturing, research and development and warehouse operations to a 55,000 square foot facility that we lease in Westford, Massachusetts. In October 2007, we amended this lease to include an additional 12,500 square feet of office space. The lease on this facility expires in December 2012. In addition, we lease an aggregate of approximately 5,300 square feet of space at six other locations in Europe and the Asia/Pacific region that we use for sales and service purposes.

Item 3. *Legal Proceedings*

In May 2005, Dr. Ari Weitzner, individually and as putative representative of a purported class, filed a complaint against us under the federal Telephone Consumer Protection Act, or TCPA, in Massachusetts Superior Court in Middlesex County seeking monetary damages, injunctive relief, costs and attorneys fees. The complaint alleges that we violated the TCPA by sending unsolicited advertisements by facsimile to the plaintiff and other recipients without the prior express invitation or permission of the recipients. Under the TCPA, recipients of unsolicited facsimile advertisements are entitled to damages of up to $500 per facsimile for inadvertent violations and up to $1,500 per facsimile for knowing or willful violations. We believe the number of unsolicited facsimiles to be quite large. The plaintiff recently filed a motion seeking class certification, which we are opposing. Until this motion is ruled on, it would be premature to speculate about our potential exposure in the case.

In December 2005, certain individuals commenced an arbitration against us along with Sona International Inc., Sona Med Spa Inc., Carousel Capital, Inc. and various individuals. The arbitration demand alleges fraud, violations of various state consumer protection laws and other causes of action in connection with the plaintiffs' acquisition of franchises from the Sona entities. We declined to participate in the arbitration because we had not agreed contractually to do so, and we have been dismissed from the arbitration by agreement of the parties.

In January 2006, Gentle Laser Solutions, Inc., Liberty Bell Med Spa, Inc. and Kevin T. Campbell filed suit against us and one of our former directors, along with Sona International Inc., Sona Lasers Centers, Inc. and various other individuals, in the Superior Court of New Jersey. The matter was later removed to the U. S. District Court in the District of New Jersey. The suit alleges fraud, breach of contract and other causes of action in connection with the plaintiffs' acquisition of franchises from the Sona entities. The plaintiffs' and Sona have settled the plaintiffs' claims against Sona. We have moved to dismiss the plaintiffs' claims against us. We are not able to estimate the amount or range of loss that could result from an unfavorable outcome of the lawsuit as the matter is still in the early stages of the proceedings.

In June 2006, Baltimore Laser Solutions, Inc. and Kevin T. Campbell, filed suit against us and one of our former directors, along with Sona International Inc., Sona Lasers Centers, Inc. and various other individuals, in the U. S. District Court in the District of Maryland. The suit alleges fraud, breach of contract and other causes of action in connection with the plaintiffs' acquisition of franchises from the Sona entities. On April 11, 2007, upon a motion by the Sona defendants, the Court dismissed the suit in its entirety, without prejudice.

On January 9, 2008, we commenced a lawsuit in the U.S. District Court for the District of Massachusetts against CoolTouch Inc. for infringement of U.S. Patent No. 6,206,873, or the 873 patent. Our complaint alleges that CoolTouch's "CoolLipo" infringes on the 873 patent and seeks damages and injunctive relief. On January 31, 2008, CoolTouch answered our complaint, denying liability and alleging that the 873 patent is not infringed and is invalid, and also asserted counterclaims against us in the same court alleging patent infringement by us. CoolTouch's counterclaim alleges that our Affirm product infringes U.S. Patent Nos. 7,122,029 and 6,451,007, and that our Smartlipo product infringes U.S. Patent No. 7,217,265, and seeks damages in an unspecified amount, as well as injunctive relief. We are vigorously prosecuting our claims against CoolTouch and defending against CoolTouch's counterclaims. We are not able to estimate the amount or range of loss that could result from an unfavorable outcome of the lawsuit as the matter is still in the early stages of the proceedings.

In addition to the matters discussed above, from time to time, we are subject to various claims, lawsuits, disputes with third parties, investigations and pending actions involving various allegations against us incident to the operation of its business, principally product liability. Each of these other matters is subject to various uncertainties, and it is possible that some of these other matters may be resolved unfavorably to us. We establish accruals for losses that management deems to be probable and subject to reasonable estimate. We believe that the ultimate outcome of these matters will not have a material adverse impact on our consolidated financial position, results of operations or cash flows.

Item 4. ***Submission of Matters to a Vote of Security Holders.***

None.

PART II

Item 5. ***Market for Registrant's Common Equity, Related Stockholder Matters and Issuers Purchases of Equity Securities***

Market Price of and Dividends on Our Common Stock and Related Stockholder Matters.

Our class A common stock trades on The Nasdaq Global Market under the symbol "CYNO." The following table sets forth, for the periods indicated, the high and low sales prices of our class A common stock on The Nasdaq Global Market.

	High	Low
Fiscal Year Ended December 31, 2006		
First quarter	$22.49	$16.94
Second quarter	$18.82	$12.96
Third quarter	$15.38	$11.38
Fourth quarter	$19.13	$13.93
Fiscal Year Ended December 31, 2007		
First quarter	$30.57	$15.85
Second quarter	$39.18	$26.11
Third quarter	$39.10	$26.14
Fourth quarter	$45.00	$25.20

There is no established public trading market for our class B common stock because, under the terms of our restated certificate of incorporation, shares of our class B common stock will convert automatically into class A common stock upon any transfer of such shares, whether or not for value. Additionally, shares of our class B common stock are also convertible into class A common stock upon the occurrence of events specified in our restated certificate of incorporation. Each share of our class B common stock is convertible into one share of class A common stock.

On March 7, 2008, the closing price per share of our class A common stock was $18.91, as reported on The Nasdaq Global Market. The number of record holders of our class A common stock as of March 7, 2008 was 10. The number of record holders of our class B common stock as of March 7, 2008 was four.

We have never paid or declared any cash dividends on our common stock. We currently intend to retain earnings, if any, to finance the growth and development of our business. Payment of future dividends, if any, will be at the discretion of our board of directors.

On December 13, 2005, we completed an initial public offering of 5,750,000 shares of our class A common stock at a price to the public of $15.00 per share. We sold 4,750,000 shares of the class A common stock, including an over-allotment option of 750,000 shares, and El.En., the selling shareholder in the offering, sold 1,000,000 of the shares. The offer and sale of all of the shares in the initial public offering were registered under the Securities Act of 1933, as amended, pursuant to a registration statement on Form S-1 (File No. 333-127463), which was declared effective by the Securities and Exchange Commission on November 8, 2005. We received aggregate net proceeds of approximately $64.0 million, after deducting underwriting discounts and commission of approximately $5.0 million and expenses of the offering of approximately $2.3 million. None of the underwriting discounts and commissions or offering expenses were incurred or paid to directors or officers of ours or their associates or to persons owning 10 percent or more of our common stock or to any affiliates of ours. From the effective date of the registration statement through December 31, 2007, we used approximately $18.4 million for general corporate purposes, with the remaining $82.4 million in proceeds invested in cash and cash equivalents and marketable securities.

Item 6. *Selected Consolidated Financial Data*

You should read the following selected consolidated financial data in conjunction with our consolidated financial statements and the related notes which are included elsewhere in this Annual Report and the "Management's Discussion and Analysis of Financial Condition and Results of Operations" section of this Annual Report. We have derived the consolidated statement of operations data for the years ended December 31, 2007, 2006 and 2005 and the consolidated balance sheet data as of December 31, 2007 and 2006 from our audited consolidated financial statements, which are included elsewhere in this Annual Report. We have derived the consolidated statement of operations data for the years ended December 31, 2004 and 2003 and the consolidated balance sheet data as of December 31, 2005, 2004 and 2003 from our audited consolidated financial statements, which are not included in this Annual Report. Our historical results for any prior period are not necessarily indicative of results to be expected for any future period.

	Year Ended December 31,				
	2007	2006	2005	2004	2003
	(In thousands, except per share data)				
Consolidated Statement of Operations Data:					
Revenues	$124,315	$ 78,401	$ 56,262	$40,364	$25,525
Revenues from related party	—	—	—	1,269	1,600
Total revenues	124,315	78,401	56,262	41,633	27,125
Cost of revenues	44,507	32,920	25,843	20,465	14,207
Gross profit	79,808	45,481	30,419	21,168	12,918
Operating expenses:					
Sales and marketing	42,058	26,213	17,506	12,627	8,752
Research and development	6,827	4,673	3,199	3,222	2,501
General and administrative	11,346	8,975	5,103	4,108	3,790
Royalty settlement	—	10,000	—	—	—
Total operating expenses	60,231	49,861	25,808	19,957	15,043
Income (loss) from operations	19,577	(4,380)	4,611	1,211	(2,125)
Interest income (expense), net	2,516	2,579	89	(122)	(62)
(Loss) gain on investments	(171)	118	—	3,019	—
Other income (expense), net	866	813	(368)	976	1,822
Income (loss) before provision for (benefit from) income taxes and minority interest	22,788	(870)	4,332	5,084	(365)
Provision for (benefit from) income taxes	8,276	(266)	102	(276)	72
Minority interest in net income of subsidiary	—	46	70	64	63
Net income (loss)	$ 14,512	$ (650)	$ 4,160	$ 5,296	$ (500)
Basic net income (loss) per share	$ 1.21	$ (0.06)	$ 0.64	$ 0.93	$ (0.09)
Diluted net income (loss) per share	$ 1.15	$ (0.06)	$ 0.54	$ 0.92	$ (0.09)
Basic weighted average common shares outstanding	11,993	11,084	6,522	5,700	5,530
Diluted weighted average common shares outstanding	12,654	11,084	7,715	5,773	5,530

	2007	2006	2005	2004	2003
Consolidated Balance Sheet Data:					
Cash, cash equivalents and marketable securities	$ 86,097	$ 57,246	$ 64,646	$ 4,028	$ 2,111
Working capital	113,732	80,460	79,227	10,678	4,572
Total assets	149,844	109,566	100,168	28,001	18,228
Capital lease obligation, net of current portion	794	1,069	814	476	81
Retained earnings (accumulated deficit)	20,332	5,820	6,470	2,310	(2,985)
Total stockholders' equity	120,878	85,870	83,151	14,640	7,283

Item 7. *Management's Discussion and Analysis of Financial Condition and Results of Operations*

Company Overview

You should read the following discussion and analysis of our financial condition and results of operations together with our financial statements and the related notes and other financial data included elsewhere in this Annual Report. Some of the information contained in this discussion and analysis or set forth elsewhere in this Annual Report, including information with respect to our plans and strategy for our business, includes forward-looking statements that involve risks and uncertainties. You should review Item 1A of this Annual Report for a discussion of important factors that could cause actual results to differ materially from the results described in or implied by the forward-looking statements contained in the following discussion and analysis.

Company Overview

We develop and market aesthetic treatment systems used by physicians and other practitioners that incorporate laser and light-based energy sources. As of December 31, 2007, we had sold more than 7,100 aesthetic treatment systems worldwide.

We were incorporated in July 1991. In 2002, El.En. S.p.A., an Italian company that itself and through subsidiaries develops and markets laser systems for medical and industrial applications, acquired a majority of our capital stock. In September 2003, we recruited a new management team that has implemented a comprehensive reorganization of our company, including:

- redesigning many of our existing products;
- introducing innovative new products and technologies;
- streamlining and rationalizing our manufacturing processes;
- reorganizing and expanding our research and development, sales and marketing and distribution capabilities; and
- enhancing our customer service network.

Since the beginning of 2004, we have introduced 13 new aesthetic treatment systems, including our six flagship products:

- the *Apogee Elite* system, our flagship product for hair removal, in March 2004;
- the *Cynergy* system, our flagship product for the treatment of vascular lesions, in February 2005;
- the *TriActive LaserDermology* system, our flagship product for the temporary reduction of the appearance of cellulite, in February 2004;
- the *Affirm system*, our flagship product for anti-aging, in April 2006; and
- the *Smartlipo system*, our flagship product for LaserBodySculpting℠ for the removal of unwanted fat, in November 2006.
- the *Accolade system*, our flagship product for the removal of pigmented lesion, in February 2008.

As a result of our product development efforts, we incurred increased research and development expenses in absolute dollars, although not as a percentage of revenues, during each of 2007 and 2006.

We have expanded our direct sales and marketing organization from 22 employees as of December 31, 2003 to 134 employees as of December 31, 2007. In addition, we have expanded our distribution relationships and have 19 distributors covering 44 countries as of December 31, 2007.

We redesigned or introduced a number of our products, including our *Apogee, Cynergy, Acclaim* and *Affirm* product families, so that they are built in a modular fashion using fewer components. We began shipping these redesigned products in the second quarter of 2005. We believe that this new approach allows our platform technology to be easily upgradeable, increases the scalability and efficiency of our production process and facilitates improvements in field service diagnosis and repair.

In 2007, we released two new *Smartlipo* workstations, the 10-watt and the 18-watt *Smartlipo* workstations, that are intended for high-volume aesthetic laser practices, allowing a physician to reduce patient treatment times for laser-assisted liposuction procedures. The 10-watt and 18-watt *Smartlipo* workstations are available as a standalone unit or as an upgrade to existing systems.

Financial Operations Overview

Revenues

We generate revenues primarily from sales of our products and parts and accessories and, to a lesser extent, from services, including product warranty revenues. In 2007, we derived approximately 97% of our revenues from sales of our products and 3% of our revenues from service. In 2006, we derived approximately 95% of our revenues from sales of our products and 5% of our revenues from service. In 2005, we derived approximately 92% of our revenues from sales of our products, 6% of our revenues from service and 2% of our revenues from a revenue sharing arrangement with Sona MedSpa, which was terminated during 2006. Generally, we recognize revenues from the sales of our products upon delivery to our customers, revenues from service contracts and extended product warranties ratably over the coverage period, revenues from service in the period in which the service occurs and revenues from our revenue sharing arrangement in the period the procedures are performed. Over the past three years, service revenues as a percentage of total revenues has decreased due to the significant increase in our product sales during this three year period. Due to our one-year service warranty provided on all sales of our systems, our service revenues have a slight lag behind such product revenues.

We sell directly in North America, four European countries, Japan and China and use distributors to sell our products in other countries where we do not have a direct presence. In 2007, we derived 36% and in 2006, we derived 44% of our revenues from sales outside North America. As of December 31, 2007, we had 66 sales employees in North America, 27 sales employees in four European countries, Japan and China and distributors that cover 44 countries. The following table provides revenue data by geographical region for the years ended December 31, 2007, 2006 and 2005:

	Percentage of Revenues Year Ended December 31,		
	2007	2006	2005
Region			
North America	64%	56%	59%
Europe	22	26	23
Asia/Pacific	10	13	12
Other	4	5	6
Total	100%	100%	100%

See Note 6 to our consolidated financial statements included in this Annual Report for revenues and asset data by geographic region.

Cost of Revenues

Our cost of revenues consists primarily of material, labor and manufacturing overhead expenses and includes the cost of components and subassemblies supplied by third party suppliers. Cost of revenues also

includes royalties incurred on products sold, service and warranty expenses, as well as salaries and personnel-related expenses, including stock-based compensation, for our operations management team, purchasing and quality control.

Sales and Marketing Expenses

Our sales and marketing expenses consist primarily of salaries, commissions and other personnel-related expenses, including stock-based compensation, for employees engaged in sales, marketing and support of our products, trade show, promotional and public relations expenses and management and administration expenses in support of sales and marketing. We expect our sales and marketing expenses to increase in absolute dollars, though we do not expect them to increase significantly as a percentage of revenues, as we expand our sales, marketing and distribution capabilities.

Research and Development Expenses

Our research and development expenses consist of salaries and other personnel-related expenses, including stock-based compensation, for employees primarily engaged in research, development and engineering activities and materials used and other overhead expenses incurred in connection with the design and development of our products. We expense all of our research and development costs as incurred. We expect our research and development expenditures to increase in absolute dollars, though we do not expect them to increase significantly as a percentage of revenues, as we continue to devote resources to research and develop new products and technologies.

General and Administrative Expenses

Our general and administrative expenses consist primarily of salaries and other personnel-related expenses, including stock-based compensation, for executive, accounting and administrative personnel, professional fees and other general corporate expenses. We expect our general and administrative expenses to increase in absolute dollars, though we do not expect them to increase significantly as a percentage of revenues.

Interest Income (Expense), net

Interest income consists primarily of interest earned on our marketable securities portfolio consisting mainly of state and municipal bonds. Interest expense consists primarily of interest due on capitalized leases.

Provision for Income Taxes

As of December 31, 2006, we maintained a full valuation allowance on all of our foreign deferred tax assets. During 2007, we made the determination that, based on the weight of all available evidence, it is now more likely than not that we will realize a tax benefit for our deferred tax assets in most of our jurisdictions. As a result, we have released the valuation allowance on the deferred tax assets in all of our foreign jurisdictions, with the exception of Germany. A tax benefit of $429,000 was realized in the foreign deferred tax provision for the release of this valuation allowance. As of December 31, 2007, we had foreign net operating loss carryforwards of approximately $2,367,000 available to reduce future foreign taxable income related to Germany, which do not expire.

Results of Operations

Year Ended December 31, 2007 and 2006

The following table contains selected statement of operations data, which serves as the basis of the discussion of our results of operations for the years ended December 31, 2007 and 2006:

	Year Ended December 31, 2007		Year Ended December 31, 2006		Change 2006 to 2007	
	Amount	As a % of Revenues	Amount	As a % of Revenues	$ Change	% Change
			(Dollars in thousands)			
Revenues	$124,315	100%	$78,401	100%	$ 45,914	59%
Cost of revenues	44,507	36	32,920	42	11,587	35
Gross profit	79,808	64	45,481	58	34,327	75
Operating expenses:						
Sales and marketing	42,058	34	26,213	33	15,845	60
Research and development	6,827	5	4,673	6	2,154	46
General and administrative	11,346	9	8,975	11	2,371	26
Royalty settlement	—	—	10,000	13	(10,000)	-100
Total operating expenses	60,231	48	49,861	63	10,370	21
Income (loss) from operations	19,577	16	(4,380)	(5)	23,957	547
Interest income, net	2,516	2	2,579	3	(63)	-2
(Loss) gain on investments	(171)	—	118	—	(289)	-245
Other income, net	866	1	813	1	53	7
Income (loss) before provision for (benefit from) income taxes and minority interest	22,788	18	(870)	(1)	23,658	2719
Provision for (benefit from) income taxes	8,276	7	(266)	—	8,542	3211
Minority interest in net income of subsidiary	—	—	46	—	(46)	-100
Net income (loss)	$ 14,512	12%	$ (650)	(1)%	$ 15,162	2333%

Revenues

Revenues in the year ended December 31, 2007 exceeded revenues in 2006 by $45.9 million, or 59%. The increase in revenues was attributable to a number of factors (in thousands, except for percentages):

	Year Ended December 31,		$	%
	2007	2006	Change	Change
Product sales in North America	$ 73,728	$39,784	$33,944	85%
Product sales outside North America	36,941	28,373	8,568	30
Original equipment manufacturer sales and revenue sharing	1,164	1,183	(19)	(2)
Parts, accessories and service sales	12,482	9,061	3,421	38
Total Revenues	$124,315	$78,401	$45,914	59%

- Revenues from the sale of products in North America increased $33.9 million, or 85%, to $73.7 million in 2007 as compared to $39.8 million in 2006. The increase was attributable to an increase in the number of product units sold and a higher average selling price due to a favorable change in product mix. The increase in North American revenues resulted in part from the reorganization and expansion of our North American sales organization, including the hiring of 20 additional direct sales employees between December 31, 2006 and 2007. The increase also resulted from the introduction of new products, particularly our *Affirm* and *Smartlipo* systems, which were introduced in late 2006.

- Revenues from sales of products outside of North America increased $8.6 million, or 30%, to $36.9 million in 2007 as compared to $28.4 million in 2006. The increase was mainly attributable to an increase in sales in Europe of $6.1 million, or 35%, over 2006, and an increase in sales in Asia/Pacific of $2.3 million, or 31%, over 2006, resulting from a favorable change in product mix and our increased focus on direct selling, for which we receive higher average selling prices as compared to sales through distributors.
- Revenues from original equipment manufacturer and other relationships and our revenue sharing arrangement remained relatively flat, year over year.
- Revenues from the sale of parts and accessories and services increased $3.4 million, or 38%, to $12.5 million in 2007 as compared to $9.1 million in 2006. The increase was primarily attributable to an increase in revenues generated from the sale of disposable components, related to our *Affirm* and *Smartlipo* systems that were introduced in late 2006, and parts. The increase also relates to an increase in revenues generated from service contracts year over year, both of which are related to the overall increase in volume of sales during the past three years.

Cost of Revenues

	Year Ended December 31,		$	%
	2007	2006	Change	Change
Cost of revenues (in thousands)	$44,507	$32,920	$11,587	35%
Cost of revenues (as a percentage of total revenues)	36%	42%		

Cost of revenues increased $11.6 million, or 35%, to $44.5 million in 2007, as compared to $32.9 million in 2006. The increase in the cost of revenues was primarily attributable to an increase in direct labor, overhead and material costs associated with increased sales of our products and royalties incurred on the sale of hair-removal systems. Included in cost of revenues for 2006 was a write off of $0.7 million related to inventory delivered under an agreement with Sona MedSpa, which was terminated in June 2006, for which there was no related expense in 2007. Our cost of revenues decreased as a percentage of revenues to 36% in 2007 from 42% in 2006, resulting in an increase in our gross margin of 6% between the two years. The improved margin resulted primarily from higher average selling prices of our products due to a favorable change in product mix, in part as a result of the introduction of our *Affirm* and *Smartlipo* systems at the end of 2006 for which there was a full year of product sales in 2007 related to these new systems, a more favorable distribution mix toward direct sales and the write-off of inventory related to Sona MedSpa.

Sales and Marketing

	Year Ended December 31,		$	%
	2007	2006	Change	Change
Sales and marketing (in thousands)	$42,058	$26,213	$15,845	60%
Sales and marketing (as a percentage of total revenues)	34%	33%		

Sales and marketing expenses increased $15.8 million, or 60%, to $42.1 million in 2007, as compared to $26.2 million in 2006. The increase was primarily attributable to an increase of $8.4 million in personnel costs and travel expenses associated with the expansion of our North American direct sales organization, which includes an increase of $4.1 million in commissions expense, an increase of $1.2 million in non-cash stock-based compensation expense, and an increase of $3.2 million in personnel costs and travel expenses associated with our international subsidiaries. Promotional costs increased $3.0 million, primarily due to our increased number of clinical workshops and trade shows, as well as other promotional efforts. As a percentage of revenues, sales and marketing expenses remained relatively consistent, with no material difference as a percentage of revenue.

Research and Development

	Year Ended December 31,		$	%
	2007	2006	Change	Change
Research and development (in thousands)	$6,827	$4,673	$2,154	46%
Research and development (as a percentage of total revenues)	5%	6%		

Research and development expenses increased $2.2 million or 46%, to $6.8 million in 2007, as compared to $4.7 million in 2006. The increase was primarily attributable to an increase of $0.5 million in personnel costs and in increase in project research costs and product engineering expenses of $0.9 million related to the ongoing development of new products and accessories. The increase is also attributable to an increase of $0.8 million in stock-based compensation expense. As a percentage of revenues, research and development expenses decreased to 5% in 2007 from 6% in 2006.

General and Administrative

	Year Ended December 31,		$	%
	2007	2006	Change	Change
General and administrative (in thousands)	$11,346	$8,975	$2,371	26%
General and administrative (as a percentage of total revenues)	9%	11%		

General and administrative expenses increased $2.4 million, or 26%, to $11.3 million in 2007, as compared to $9.0 million in 2006. The increase was primarily attributable to an increase of $1.3 million in personnel costs and an increase of $1.0 million in stock-based compensation expense. As a percentage of revenues, general and administrative expenses decreased to 9% in 2007 from 11% in 2006.

Royalty Settlement

On November 6, 2006, we entered into a patent cross-license agreement with Palomar Medical Technologies, Inc. Under the cross-license agreement, we obtained a non-exclusive license to integrate into our products certain hair removal technology covered by specified U.S. and foreign patents held by Palomar and Palomar obtained certain specified U.S. and foreign patents held by us. In November 2006, we made a payment to Palomar of $10 million for royalties related to sales prior to October 1, 2006 of hair removal-only systems including our Apogee family of products, *PhotoLight*, *Acclaim 7000* and the *PhotoSilk Plus*. This was recorded as a royalty settlement within our operating expenses for the year ended December 31, 2006. In connection with this agreement, we also agreed to pay royalties to Palomar on our sales of certain hair-removal products beginning October 1, 2006. The royalty rate for sales of hair-removal products ranges from 3.75% to 7.5% of net sales, depending upon product configuration and the number of energy sources. Royalty expense associated with such sales is recorded as cost of revenues.

Interest Income, net; (Loss) Gain on Investment and Other Income, net

	Year Ended December 31,		$	%
	2007	2006	Change	Change
Interest income, net (in thousands)	$2,516	$2,579	$ (63)	-2%
(Loss) gain on investment (in thousands)	(171)	118	(289)	-245%
Other income, net (in thousands)	866	813	53	7%

Interest income (expense), net remained relatively consistent, year over year due to increases in interest income from increased cash balances available for investment offset by decreases in investment yields as a result of transitioning our investment portfolio from investments in taxable securities to investments in tax-free securities. In 2007, we recognized a net loss of $0.2 million due to an impairment loss on the value of the securities received in 2006 in connection with the sale of our investment in Solx for which we recognized a gain of $0.1 million in 2006. Other income increased to $0.9 million in 2007 from $0.8 million in 2006. The increase was partially attributable to the increase in foreign currency remeasurement gains, year over year.

Provision for (Benefit from) Income Taxes

	Year Ended December 31,		$	%
	2007	2006	Change	Change
Provision for (benefit from) income taxes (in thousands)	$8,276	$(266)	$8,542	3211%
Provision (benefit) as a percentage of income (loss) before provision for (benefit from) income taxes and minority interest	36%	(31)%		

The provision for income taxes results from a combination of activities of both the domestic and foreign subsidiaries. In 2007, we recorded an income tax provision of $8.3 million, representing an effective tax rate of 36%. In 2006, we recorded an income tax benefit of $0.3 million, representing an effective tax rate of 31%. The increase in our effective tax rate was due to a provision for income taxes of $702,000 recorded in 2007 primarily related a one-time intercompany bad debt deduction claimed in error that was identified as a result of our 2003 U.S. IRS examination, which was settled in December 2007. We concluded the effect of this error was not material to our financial statements for the years ended December 31, 2004, 2005 and 2006 and, as such, these financial statements were not restated. We also concluded that providing for the correction of the error in 2007 would not have a material effect on our financial statements for the year ended December 31, 2007. The increase in the effective tax rate related to the additional provision noted previously, was partially offset by the reduction in foreign tax rates, the mixture of jurisdictional earnings, and the recognition of previously unbenefited deferred tax assets. In 2006, we recorded a benefit related to net operating losses generated in 2006, which offsets the provision for current taxable income. Additionally, although we had an income tax provision of $8.3 million in 2007, we had no current U.S. federal income taxes payable due to the benefit from stock option exercises.

Year Ended December 31, 2006 and 2005

The following table contains selected statement of operations data, which serves as the basis of the discussion of our results of operations for the years ended December 31, 2006 and 2005:

	Year Ended December 31, 2006		Year Ended December 31, 2005		Change 2005 to 2006	
	Amount	As a % of Revenues	Amount	As a % of Revenues	$ Change	% Change
	(Dollars in thousands)					
Revenues	$78,401	100%	$56,262	100%	$22,139	39%
Cost of revenues	32,920	42	25,843	46	7,077	27
Gross profit	45,481	58	30,419	54	15,062	50
Operating expenses:						
Sales and marketing	26,213	33	17,506	31	8,707	50
Research and development	4,673	6	3,199	6	1,474	46
General and administrative	8,975	11	5,103	9	3,872	76
Royalty settlement	10,000	13	—	—	10,000	—
Total operating expenses	49,861	63	25,808	46	24,053	93
(Loss) income from operations	(4,380)	(5)	4,611	8	(8,991)	-195
Interest income (expense), net	2,579	3	89	—	2,490	2798
Gain on sale of investment	118	—	—	—	118	—
Other income (expense), net	813	1	(368)	(1)	1,181	321
(Loss) income before (benefit from) provision for income taxes and minority interest	(870)	(1)	4,332	7	(5,202)	-120
(Benefit from) provision for income taxes	(266)	—	102	—	(368)	-361
Minority interest in net income of subsidiary	46	—	70	—	24	34
Net (loss) income	$ (650)	(1)%	$ 4,160	7%	$ (4,810)	-116%

Revenues

Revenues in the year ended December 31, 2006 exceeded revenues in 2005 by $22.1 million, or 39%. The increase in revenues was attributable to a number of factors (in thousands, except for percentages):

	Year Ended December 31,		$	%
	2006	2005	Change	Change
Product sales in North America	$39,784	$27,803	$11,981	43%
Product sales outside North America	28,373	17,656	10,717	61
Original equipment manufacturer sales and revenue sharing	1,183	3,792	(2,609)	(69)
Parts, accessories and service sales	9,061	7,011	2,050	29
Total Revenues	$78,401	$56,262	$22,139	39%

- Revenues from the sale of products in North America increased $12.0 million, or 43%, to $39.8 million in 2006 as compared to $27.8 million in 2005. The increase was attributable to an increase in the number of product units sold and a higher average selling price due to a favorable change in product mix. The increase in North American revenues resulted in part from the reorganization and expansion of our North American sales organization, including the hiring of 21 additional direct sales employees between December 31, 2005 and 2006. The increase also resulted from the introduction of new products, particularly our *Affirm* system at the end of the third quarter of 2006. Revenues from sales of products introduced since 2004 totaled $38.4 million, or 97%, of total North American product revenues in 2006.

- Revenues from sales of products outside of North America increased $10.7 million, or 61%, to $28.4 million in 2006 as compared to $17.7 million in 2005. The increase was mainly attributable to an increase in sales in Europe of $6.6 million, or 62%, over 2005, and an increase in sales in Asia/Pacific of $3.1 million, or 74%, over 2005, resulting from a favorable change in product mix and our increased focus on direct selling, for which we receive higher average selling prices as compared to sales through distributors.
- Revenues from original equipment manufacturer and other relationships and our revenue sharing arrangement decreased $2.6 million, or 69%, to $1.2 million in 2006 as compared to $3.8 million in 2005. The decrease was mainly attributable to approximately $2.5 million of revenue generated during 2005 under a revenue sharing arrangement with Sona MedSpa for which there was no corresponding revenue generated during 2006, as the agreement was terminated in June 2006.
- Revenues from the sale of parts and accessories and services increased $2.1 million, or 30%, to $9.1 million in 2006 as compared to $7.0 million in 2005. The increase was primarily attributable to an increase of approximately $1.3 million in revenues generated from the sale of parts and an increase of approximately $0.7 million in revenues generated from service contracts year over year, both of which are related to the overall increase in volume of sales during the past three years.

Cost of Revenues

	Year Ended December 31,		$	%
	2006	2005	Change	Change
Cost of revenues (in thousands)	$32,920	$25,843	$7,077	27%
Cost of revenues (as a percentage of total revenues)	42%	46%		

Cost of revenues increased $7.1 million, or 27%, to $32.9 million in 2006, as compared to $25.8 million in 2005. The increase in the cost of revenues was primarily attributable to an increase in direct labor, overhead and material costs associated with increased sales of our products and royalties incurred on the sale of hair-removal systems. Included in cost of revenues for 2006 was a write off of $0.7 million related to inventory delivered under our agreement with Sona MedSpa, which was terminated in June 2006, as previously discussed, for which there was no related expense in 2005. Our cost of revenues decreased as a percentage of revenues to 42% in 2006 from 46% in 2005, resulting in an increase in our gross margin of 4% between the two years. The improved margin resulted primarily from higher average selling prices of our products due to a favorable change in product mix, in part as a result of the introduction of our *Affirm* system at the end of the third quarter of 2006, as well as increased direct sales in North America. We derived all of our North American product revenues from direct sales.

Sales and Marketing

	Year Ended December 31,		$	%
	2006	2005	Change	Change
Sales and marketing (in thousands)	$26,213	$17,506	$8,707	50%
Sales and marketing (as a percentage of total revenues)	33%	31%		

Sales and marketing expenses increased $8.7 million, or 50%, to $26.2 million in 2006, as compared to $17.5 million in 2005. The increase was primarily attributable to an increase of $4.4 million in personnel costs and travel expenses associated with the expansion of our North American direct sales organization, which includes an increase of $2.1 million in commissions expense, an increase of $0.4 million in non-cash stock-based compensation expense related to the adoption of SFAS No. 123(R), and an increase of $0.5 million in personnel

costs and travel expenses associated with our international subsidiaries. Promotional costs increased $1.9 million, primarily due to our increased number of clinical workshops and trade shows, as well as an increase in clinical studies costs and promotional efforts. Consulting and outside services expenses have increased by $1.5 million. As a percentage of revenues, sales and marketing expenses increased to 33% in 2006 from 31% in 2005.

Research and Development

	Year Ended December 31,		$	%
	2006	2005	Change	Change
Research and development (in thousands)	$4,673	$3,199	$1,474	46%
Research and development (as a percentage of total revenues)	6%	6%		

Research and development expenses increased $1.5 million or 46%, to $4.7 million in 2006, as compared to $3.2 million in 2005. In 2006, our research and development expenses were attributable to project research costs and product engineering expenses related to the introduction of our new *Affirm* system in the third quarter of 2006 and ongoing development of new products. In 2005, our research and development expenses were attributable to project research costs and product engineering expenses related to the introduction of our new *Cynergy* system in the first quarter of 2005 and ongoing development of new products. The increase is also attributable to an increase of $0.6 million in non-cash stock-based compensation expense related to the adoption of SFAS No. 123(R). As a percentage of revenues, research and development expenses remained relatively flat at 6% in 2006 and 2005.

General and Administrative

	Year Ended December 31,		$	%
	2006	2005	Change	Change
General and administrative (in thousands)	$8,975	$5,103	$3,872	76%
General and administrative (as a percentage of total revenues)	11%	9%		

General and administrative expenses increased $3.9 million, or 76%, to $9.0 million in 2006 from $5.1 million in 2005. The increase was primarily attributable to costs associated with being a public company, which included a $1.7 million increase in consulting, legal and professional service fees, related to legal, audit and tax service fees, as well as consulting service fees related to the implementation of the internal control compliance and reporting requirements of Section 404 of the Sarbanes-Oxley Act of 2002, and a $0.7 million increase in personnel-related costs. The increase is also attributable to an increase of $0.9 million in stock-based compensation expense related to the adoption of SFAS No. 123(R). Bad debt expense has increased by $0.6 million due to the settlement of arbitration with Sona MedSpa and the write off of certain receivable balances related to the preferred vendor and revenue sharing agreements with this party, which were terminated in June 2006. As a percentage of revenues, general and administrative expenses increased to 11% in 2006 from 9% in 2005.

Royalty Settlement

On November 6, 2006, we entered into a patent cross-license agreement with Palomar Medical Technologies, Inc. Under the cross-license agreement, we obtained a non-exclusive license to integrate into our products certain hair removal technology covered by specified U.S. and foreign patents held by Palomar and Palomar obtained certain specified U.S. and foreign patents held by us. In November 2006, we made a payment to Palomar of $10 million for royalties related to sales prior to October 1, 2006 of hair removal-only systems including our Apogee family of products, *PhotoLight*, *Acclaim 7000* and the *PhotoSilk Plus*. This was recorded

as a royalty settlement within our operating expenses for the year ended December 31, 2006. In connection with this agreement, we also agreed to pay royalties to Palomar on our sales of certain hair-removal products beginning October 1, 2006. The royalty rate for sales of hair-removal products ranges from 3.75% to 7.5% of net sales, depending upon product configuration and the number of energy sources. Royalty expense associated with such sales is recorded as cost of revenues.

Interest Income, net; Gain on Sale of Investment and Other Income (Expense), net

	Year Ended December 31,		$	%
	2006	2005	Change	Change
Interest income, net (in thousands)	$2,579	$ 89	$2,490	2798%
Gain on sale of investment (in thousands)	118	—	118	—
Other income (expense), net (in thousands)	813	(368)	1,181	321%

Interest income, net increased to $2.6 million in 2006 from $89,000 in 2005. The increase resulted from interest earned on increased cash balances available for investment due to our initial public offering in December 2005. In 2006, we recorded a gain of $0.1 million on the sale of our equity interest in Solx, Inc. to a public company in exchange for consideration in cash and shares of common stock in the acquiring company. We had no similar gain in 2005. Other income (expense) increased to $0.8 million in income in 2006 from $0.4 million in expense in 2005. The increase was partially attributable to an increase in foreign currency remeasurement gains during 2006, as compared to foreign currency remeasurement losses during 2005.

(Benefit from) Provision for Income Taxes

	Year Ended December 31,		$	%
	2006	2005	Change	Change
(Benefit from) provision for income taxes (in thousands)	$(266)	$102	$(368)	(361)%
(Benefit) provision as a percentage of (loss) income before (benefit from) provision for income taxes and minority interest	(31)%	2%		

In 2006, we recorded an income tax benefit of $0.3 million, representing an effective tax rate of 31%. In 2005, we recorded an income tax provision of $0.1 million, representing an effective tax rate of 2%. In 2006, we recorded a benefit related to net operating loss carryforwards generated in 2006, which offsets the provision for current taxable income. In 2005, we reduced the valuation allowance related to certain temporary differences and recorded a deferred tax asset of approximately $1.3 million as realization of these assets became probably in 2005 based on our future projections of our taxable income.

Liquidity and Capital Resources

We require cash to pay our operating expenses, make capital expenditures and pay our long-term liabilities. Since our inception, we have funded our operations through private placements of equity securities, short-term borrowings and funds generated from our operations. In December 2005, we completed our initial public offering of 5,750,000 shares of our class A common stock at a price to the public of $15.00 per share. We sold 5,750,000 shares of our class A common stock, including an over-allotment option of 750,000 shares. We received aggregate net proceeds of approximately $64.0 million, after deducting underwriting discounts and commission of approximately $5.0 million and expenses of the offering of approximately $2.3 million.

At December 31, 2007, our cash, cash equivalents and marketable securities were $86.1 million as compared to $57.2 million at December 31, 2006. Our cash and cash equivalents of $39.0 million are highly liquid investments with maturity of 90 days or less at date of purchase and consist of time deposits and

investments in money market funds with commercial banks and financial institutions. Our marketable securities of $47.1 million consist of investments in various state and municipal governments all of which mature by July 1, 2009.

Commencing on February 13, 2008, certain Auction Rate Securities ("ARS") that we hold experienced failed auctions that limited the liquidity of these securities. Based on current market conditions, it is likely that auction failures will continue that could result in either temporary or other-than-temporary impairments of our ARS holdings, which totaled $26.3 million of February 28, 2008. We have the ability and intent to hold these securities until a successful auction occurs and the ARSs are liquidated at par value. If in the future we determine that any decline in value of the ARSs is other-than-temporary, we would be required to recognize the loss in our statement of operations, which could have a material impact on our operating results in the period it is recognized. Further, as the funds associated with the ARSs may not be accessible for longer than twelve months because of continued failed auctions or our inability to find a buyer outside of the auction process, we may classify these securities as long-term assets in our consolidated balance sheet as of March 31, 2008, or thereafter.

Our future capital requirements depend on a number of factors, including the rate of market acceptance of our current and future products, the resources we devote to developing and supporting our products and continued progress of our research and development of new products. We expect our capital expenditures over the next 12 months generally to be consistent with our capital expenditures during the prior 12 months.

We believe that our current cash, cash equivalents and marketable securities, as well as cash generated from operations, will be sufficient to meet our anticipated cash needs for working capital and capital expenditures for the foreseeable future.

Cash Flows

Net cash provided by operating activities was $21.4 million for the year ended December 31, 2007. This resulted primarily from net income for the period of $14.5 million, increased by approximately $8.6 million in depreciation and stock-based compensation expense and decreased by approximately $1.8 million in deferred income tax benefits. Net changes in working capital items decreased cash from operating activities by approximately $0.4 million principally related to an increase in inventory for anticipated future sales and an increase in accounts receivable reflecting the record sales during the fourth quarter of 2007, offset by an increase in accrued expenses. Net cash used in investing activities was $8.2 million for the year ended December 31, 2007, which consisted primarily of $72.1 million used to purchase marketable securities, offset by $68.2 million in proceeds generated from sales and maturities of securities, $4.2 million used for fixed asset purchases. Net cash provided by financing activities during the year ended December 31, 2007 was $12.8 million, principally relating to proceeds from option exercises of $6.1 million, tax benefits related to stock options of $7.4 million and offset by $0.4 million in payments on capital lease obligations.

Net cash used in operating activities was $4.1 million for the year ended December 31, 2006. This resulted primarily from net loss for the period of $0.7 million, increased by approximately $4.9 million in depreciation and stock-based compensation expense and decreased by approximately $1.1 million in deferred income tax benefits and $0.6 million in accretion of discounts on marketable securities. Net changes in working capital items decreased cash from operating activities by approximately $6.7 million principally related to the $10.0 million payment to Palomar during 2006, an increase in inventory for anticipated future sales and an increase in accounts receivable reflecting the record sales during the fourth quarter of 2006. Net cash used in investing activities was $46.6 million for the year ended December 31, 2006, which consisted primarily of $138.9 million used to purchase marketable securities, offset by $145.9 million in proceeds generated from sales and maturities of securities, $3.2 million used for fixed asset purchases and $0.6 million used to purchase the remaining minority interest in Suzhou Cynosure Medical Devices, Co. Net cash provided by financing activities during the year ended December 31, 2006 was $0.5 million, principally relating to proceeds from option exercises of $0.5 million, tax benefits related to stock options of $0.4 million and offset by $0.4 million in payments on capital lease obligations.

Net cash used in operating activities was $1.0 million for the year ended December 31, 2005. This resulted primarily from net income for the period of $4.2 million increased by approximately $2.2 million in depreciation and stock-based compensation expense and decreased by approximately $1.9 million in deferred income tax benefits. Net changes in working capital items decreased cash from operating activities by approximately $5.5 million principally related to an increase in inventory for anticipated future sales and in preparation for our transition to modular assembly and contract manufacturing. Net cash used in investing activities was $2.4 million for the year ended December 31, 2005 resulting primarily from $2.8 million used for fixed asset purchases and the payment of a $0.2 million security deposit relating to the lease for our new corporate headquarters offset by the receipt of $0.5 million released from escrow as part of the sale of our investment in Sona MedSpa. Net cash provided by financing activities was $63.6 million for the year ended December 31, 2005 resulting primarily from net proceeds of $64.0 million from our initial public offering offset by repayment of $0.3 million of a note payable to a related party.

Contractual Obligations

Our major outstanding contractual obligations relate to our capital leases from equipment financings and our facilities leases. In addition, we guaranteed the lease obligations for two facilities that are operated by Sona MedSpa and will be obligated to pay these leases if Sona MedSpa can not or does not make the required lease payments. We have summarized in the table below our fixed contractual cash obligations as of December 31, 2007.

	Total	Less Than One Year	One to Three Years	Three to Five Years	More than Five Years
			(In thousands)		
Capital lease obligations, including interest	$1,519	$ 596	$ 765	$ 158	$ —
Operating leases	5,713	1,203	2,151	2,359	—
Lease guarantees	157	54	84	19	—
Total contractual obligations	$7,389	$1,853	$3,000	$2,536	$ —

Off Balance Sheet Arrangements

Since inception, we have not engaged in any off balance sheet financing activities.

Critical Accounting Policies and Estimates

The discussion and analysis of our financial condition and results of operations set forth above are based on our financial statements, which have been prepared in accordance with U.S. generally accepted accounting principles. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses. On an ongoing basis, we evaluate our estimates and judgments, including those described below. We base our estimates on historical experience and on various assumptions that we believe to be reasonable under the circumstances. These estimates and assumptions form the basis for making judgments about the carrying values of assets and liabilities, and the reported amounts of revenues and expenses, that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

We believe the following critical accounting policies require significant judgment and estimates by us in the preparation of our financial statements.

Revenue Recognition and Deferred Revenue

In accordance with Staff Accounting Bulletin No. 104, *Revenue Recognition in Financial Statements*, we recognize revenue from sales of aesthetic treatment systems and accessories when each of the following four criteria are met:

- delivery has occurred;
- there is persuasive evidence of an agreement;
- the fee is fixed or determinable; and
- collection is reasonably assured.

Revenue from the sale of service contracts is deferred and recognized on a straight-line basis over the contract period as services are provided. We are party to a revenue sharing arrangement with an operator and franchisor of spa franchises and recognize revenue from this arrangement in the period in which the procedures are performed.

We defer, until earned, payments that we receive in advance of product delivery or performance of services. When we enter into arrangements with multiple elements, which may include sales of products together with service contracts and warranties, we allocate revenue among the elements based on each element's fair value in accordance with the principles of Emerging Issues Task Force Issue Number 00-21, *Revenue Arrangements with Multiple Deliverables*. This allocation requires us to make estimates of fair value for each element.

Accounts Receivable and Concentration of Credit Risk

Our accounts receivable balance, net of allowance for doubtful accounts, was $24.1 million as of December 31, 2007, compared with $19.9 million as of December 31, 2006. The allowance for doubtful accounts as of December 31, 2007 was $1.5 million and as of December 31, 2006 was $1.0 million. We maintain an allowance for doubtful accounts based upon the aging of our receivable balances, known collectibility issues and our historical experience with losses. While our credit losses have historically been within our expectations and the allowances established, we may not continue to experience the same credit losses that we have in the past, which could cause our provisions for doubtful accounts to increase. We work to mitigate bad debt exposure through our credit evaluation policies, reasonably short payment terms and geographical dispersion of sales. Our revenues include export sales to foreign companies located principally in Europe, the Asia/Pacific region and the Middle East. We obtain letters of credit for foreign sales that we consider to be at risk.

Inventories and Allowance for Obsolescence

We state all inventories at the lower of cost or market value, determined on a first-in, first-out method. We monitor standard costs on a monthly basis and update them annually and as necessary to reflect changes in raw material costs and labor and overhead rates. Our inventory balance was $22.4 million as of December 31, 2007 compared to $17.6 million as of December 31, 2006. Our inventory allowance as of December 31, 2007 was $1.6 million and as of December 31, 2006 was $1.0 million. We provide inventory allowances when conditions indicate that the selling price could be less than cost due to physical deterioration, usage, obsolescence, reductions in estimated future demand and reductions in selling prices. We balance the need to maintain strategic inventory levels with the risk of obsolescence due to changing technology and customer demand levels. Unfavorable changes in market conditions may result in a need for additional inventory reserves that could adversely impact our gross margins. Conversely, favorable changes in demand could result in higher gross margins when we sell products.

Product Warranty Costs and Provisions

We provide a one-year parts and labor warranty on end-user sales of our aesthetic treatment systems. Distributor sales generally include a warranty on parts only. We estimate and provide for future costs for initial product warranties at the time revenue is recognized. We base product warranty costs on related material costs, technical support labor costs and overhead. We provide for the estimated cost of product warranties by considering historical material, labor and overhead expenses and applying the experience rates to the outstanding warranty period for products sold. As we sell new products to our customers, we must exercise considerable judgment in estimating the expected failure rates and warranty costs. If actual product failure rates, material usage, service delivery costs or overhead costs differ from our estimates, we would be required to revise our estimated warranty liability.

Stock-Based Compensation

Prior to January 1, 2006, we accounted for stock-based awards under the recognition and measurement provisions of Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees*, and related Interpretations, as permitted by Financial Accounting Standards Board Statement No. 123, *Accounting for Stock-Based Compensation*, or SFAS 123. Effective January 1, 2006, we adopted the fair value recognition provisions of FASB Statement No. 123(R), *Share-Based Payment*, or SFAS 123(R), using the modified-prospective-transition method. The modified-prospective-transition method is one in which compensation cost is recognized beginning with the effective date (1) for all share-based payments granted after the effective date and (2) for all awards granted to employees prior to the effective date of SFAS 123(R) that remain unvested on the effective date. In addition, SFAS 123(R) requires companies to utilize an estimated forfeiture rate when calculating the expense for the period, whereas, SFAS 123 permitted companies to record forfeitures based on actual forfeitures, which was our historical policy under SFAS 123.

During the year ended December 31, 2006, we applied an estimated annual forfeiture rate of 1% in determining the expense recorded in the consolidated statements of income. Upon review of our actual rate of forfeitures since the adoption of SFAS 123(R), and in consideration of management's expectations for future forfeitures, we changed our estimated annual forfeiture rate in 2007 from 1% to 5%. This change in estimate was applied retrospectively and we recorded a cumulative catch-up adjustment of approximately $313,000 as a reduction in stock-based compensation expense during the year ended December 31, 2007.

Option-pricing models require the input of various subjective assumptions, including the option's expected life and the price volatility of the underlying stock. Due to our initial public offering in December 2005, we believe there is not adequate information on the volatility of our own shares. As such, our estimated expected stock price volatility is based on a weighted-average of our own historic volatility and the average volatility of other similar companies in the same industry. We believe this is more reflective and a better indicator of the expected future volatility, than using an average of a comparable market index or of a comparable company in the same industry. Our expected term of options granted since adoption of SFAS 123(R) was derived from the short-cut method described in SEC's Staff Accounting Bulletin No. 107. The risk-free rate for the expected term of the option is based on the U.S. Treasury yield curve in effect at the time of grant. The dividend yield of zero is based on the fact that we have never paid cash dividends and have no present intention to pay cash dividends.

We account for transactions in which services are received from non-employees in exchange for equity instruments based on the fair value of such services received or of the equity instruments issued, whichever is more reliably measured, in accordance with SFAS No. 123(R) and the Emerging Issues Task Force Issue No. 96-18, *Accounting for Equity Instruments that are Issued to Other than Employees for Acquiring, or in Conjunction with Selling, Goods or Services*, or EITF Issue No. 96-18.

Income Taxes

We account for income taxes in accordance with SFAS No. 109, *Accounting for Income Taxes.* Under this method, we determine deferred tax assets and liabilities based upon the differences between the financial statement carrying amounts and the tax bases of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to affect taxable income. The tax consequences of most events recognized in the current year's financial statements are included in determining income taxes currently payable. However, because tax laws and financial accounting standards differ in their recognition and measurement of assets, liabilities, equity, revenues, expenses, gains and losses, differences arise between the amount of taxable income and pretax financial income for a year and between the tax bases of assets or liabilities and their reported amounts in the financial statements. Because we assume that the reported amounts of assets and liabilities will be recovered and settled, respectively, a difference between the tax basis of an asset or a liability and its reported amount in the balance sheet will result in a taxable or a deductible amount in some future years when the related liabilities are settled or the reported amounts of the assets are recovered, giving rise to a deferred tax asset. We then assess the likelihood that our deferred tax assets will be recovered from future taxable income and, to the extent we believe that recovery is not likely, we establish a valuation allowance.

We adopted the provisions of FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes, an Interpretation of FAS 109, Accounting for Income Taxes,* (FIN 48) on January 1, 2007. FIN 48 clarifies the accounting for income taxes, by prescribing a minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. FIN 48 also provides guidance on derecognition, measurement, classification, interest and penalties, accounting in interim periods, disclosure and transition.

We generally report tax positions in our financial statements as they are reported on tax returns as filed or to be filed. A tax benefit is reflected in the financial statements only if it is "more-likely-than-not" that we will be able to sustain the tax position, based on its technical merits. Tax benefits from uncertain tax positions that reduce current or future income tax liabilities are reported in the financial statements only to the extent each benefit is recognized and measured, in accordance with the provisions of FIN 48. As a result of adopting FIN 48, we determined that no material cumulative effect adjustment was necessary to the opening balance of retained earnings as of January 1, 2007. We further determined, based on our analysis, that there were no significant unrecognized tax benefits that, if recognized, would affect the effective tax rate for the year ended December 31, 2007.

Recent Accounting Pronouncements

In September 2006, the FASB issued Statement No. 157, *Fair Value Measurements*, (SFAS 157). SFAS 157 defines fair value, establishes a framework for measuring fair value in accordance with generally accepted accounting principles, and expands disclosures about fair value measurements. This Statement does not require any new fair value measurements; rather, it applies under other accounting pronouncements that require or permit fair value measurements. The provisions of this Statement are to be applied prospectively as of January 1, 2008, with any transition adjustment recognized as a cumulative-effect adjustment to the opening balance of retained earnings. We do not expect that the adoption of SFAS 157 will have a material impact on our financial position or results of operations.

In February 2007, the FASB issued Statement No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities—Including an Amendment of FASB Statement No. 115* (SFAS 159), in order to permit entities to choose to measure many financial instruments and certain other eligible items at fair value at specified election dates and, thereby, mitigate volatility in reported earnings caused by measuring related assets and liabilities differently. Unrealized gains and losses on items for which the fair value option has been elected shall be reported in earnings. The provisions of SFAS 159 are to be applied prospectively as of January 1, 2008; however early adoption is permitted, subject to certain restrictions, as defined. SFAS 159 does not affect any existing accounting literature that requires certain assets and liabilities to be carried at fair value. We do not expect that the adoption of SFAS 159 will have a material impact on our financial position or results of operations.

In December 2007, the FASB issued Statement No. 141(R), *Applying the Acquisition Method* (SFAS 141(R)), which replaces FASB Statement No. 141, *Business Combinations*. This Statement retains the fundamental requirements in Statement 141 that the acquisition method of accounting (which Statement 141 called the purchase method) be used for all business combinations and for an acquirer to be identified for each business combination. This Statement defines the acquirer as the entity that obtains control of one or more businesses in the business combination and establishes the acquisition date as the date that the acquirer achieves control. Statement 141 did not define the acquirer, although it included guidance on identifying the acquirer, as does this Statement. This Statement's scope is broader than that of Statement 141, which applied only to business combinations in which control was obtained by transferring consideration. By applying the same method of accounting—the acquisition method—to all transactions and other events in which one entity obtains control over one or more other businesses, this Statement improves the comparability of the information about business combinations provided in financial reports. SFAS 141(R) applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. We do not expect that the adoption of SFAS 141(R) will have a material impact on our financial position or results of operations.

In December 2007, the FASB issued Statement No. 160, *Noncontrolling Interests in Consolidated Financial Statements—an amendment of ARB No. 51* (SFAS 160), which applies to all entities that prepare consolidated financial statements, except not-for-profit organizations, but will affect only those entities that have an outstanding noncontrolling interest in one or more subsidiaries or that deconsolidate a subsidiary. This Statement amends ARB 51 to establish accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. It clarifies that a noncontrolling interest in a subsidiary is an ownership interest in the consolidated entity that should be reported as equity in the consolidated financial statements. SFAS 160 is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008. Earlier adoption is prohibited. SFAS 160 shall be applied prospectively as of the beginning of the fiscal year in which this Statement is initially applied, except for the presentation and disclosure requirements. The presentation and disclosure requirements shall be applied retrospectively for all periods presented. We do not expect that the adoption of SFAS 160 will have a material impact on our financial position or results of operations.

Item 7A. *Quantitative and Qualitative Disclosures About Market Risk*

The following discussion about our market risk disclosures involves forward-looking statements. Actual results could differ materially from those projected in the forward-looking statements. We are exposed to market risk related to changes in interest rates and foreign currency exchange rates. We do not use derivative financial instruments.

Interest Rate Sensitivity. Our marketable securities portfolio, which totaled $47.1 million at December 31, 2007, includes Auction Rate Securities ("ARS") of $29.3 million from various issuers collateralized by student loans and municipal debt. ARSs are securities with long-term contractual maturities but with interest rates that are reset every seven to thirty-five days by auctions. At the end of each reset period, investors can sell or continue to hold the securities at par. On February 13, 2008, certain ARSs that we hold experienced failed auctions that limited the liquidity of these securities. Based on current market conditions, it is likely that auction failures will continue that could result in either temporary or other-than-temporary impairments of our ARS holdings. We have the ability and intent to hold these securities until a successful auction occurs and the ARSs are liquidated at par value. If in the future we determine that any decline in value of the ARSs is other-than-temporary, we would be required to recognize the loss in our statement of operations, which could have a material impact on our operating results in the period it is recognized. Further, as the funds associated with the ARSs may not be accessible for longer than twelve months because of continued failed auctions or our inability to find a buyer outside of the auction process, we may classify these securities as long-term assets in our consolidated balance sheet as of March 31, 2008, or thereafter.

The following table provides information about our investment portfolio. For investment securities, the table presents principal cash flows (in thousands) and weighted average interest rates by expected maturity dates.

	December 31,		
	2007	2008	2009
Investments (at fair value)	$47,076	$44,481	$2,595
Weighted average interest rate	5.23%	5.23%	5.27%

Foreign Currency Exchange. A significant portion of our operations is conducted through operations in countries other than the United States. Revenues from our international operations that were recorded in U.S. dollars represented approximately 46% of our total international revenues during the year ended December 31, 2007. Substantially all of the remainder of our revenues was from sales in euros, British pounds and Japanese yen. Since we conduct our business in U.S. dollars, our main exposure, if any, results from changes in the exchange rate between these currencies and the U.S. dollar. Our functional currency is the U.S. dollar. Our policy is to reduce exposure to exchange rate fluctuations by having most of our assets and liabilities, as well as most of our revenues and expenditures, in U.S. dollars, or U.S. dollar linked. Therefore, we believe that the potential loss that would result from an increase or decrease in the exchange rate is immaterial to our business and net assets.

Item 8. *Financial Statements and Supplementary Data*

All financial statements and schedules required to be filed hereunder are included beginning on page F-1 and are incorporated in this report by reference

Item 9. *Changes in and Disagreements with Accountants on Accounting and Financial Disclosure*

None.

Item 9A. *Controls and Procedures*

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our chief executive officer and chief financial officer, evaluated the effectiveness of our disclosure controls and procedures as of December 31, 2007. The term "disclosure controls and procedures," as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act, means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company's management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on the evaluation of our disclosure controls and procedures as of December 31, 2007, our chief executive officer and chief financial officer concluded that, as of such date, our disclosure controls and procedures were effective at the reasonable assurance level.

Changes in Internal Control over Financial Reporting

No change in our internal control over financial reporting occurred during the fiscal quarter ended December 31, 2007 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Management's Annual Report on Internal Control over Financial Reporting

Management is responsible for establishing and maintaining adequate control over financial reporting as defined in Rule 13(a)-15(f) and 15(d)-15(f) under the Exchange Act. Internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP. Internal control over financial reporting includes those policies and procedures that: 1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; 2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with GAAP, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and 3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, a system of internal control over financial reporting can provide only reasonable assurance and may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management assessed the effectiveness of our internal control over financial reporting as of December 31, 2007. In making its assessment, management used the criteria set forth in *Internal Control–Integrated Framework* issued by the Committee of Sponsoring Organizations ("COSO") of the Treadway Commission. A "material weakness" is a control deficiency (within the meaning of Public Company Accounting Oversight Board Auditing Standard No. 2), or combination of control deficiencies, that result in there being more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected on a timely basis by employees in the normal course of their assigned functions. Based on management's assessment, management determined that the Company maintained effective internal control over financial reporting as of December 31, 2007 based on the COSO criteria.

Our internal control over financial reporting as of December 31, 2007 has been audited by Ernst & Young, LLP, an independent registered public accounting firm, as stated in its report below.

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders of
Cynosure, Inc.:

We have audited Cynosure Inc.'s internal control over financial reporting as of December 31, 2007, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). Cynosure, Inc.'s management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Annual Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Cynosure, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2007, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets as of December 31, 2007 and 2006, and the related consolidated statements of operations, stockholders' equity and comprehensive income (loss) and cash flows for each of the three years in the period ended December 31, 2007 of Cynosure, Inc. and our report dated March 11, 2008 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Boston, Massachusetts
March 11, 2008

Item 9B. ***Other Information***

In October 2007, we entered into Amendment No. 1 to the Lease, dated January 31, 2005, with Glenborough Fund V, Limited Partnership. Under the amendment, we agreed to lease an additional 12,500 square feet of office space, and we extended the term of the lease to December 31, 2012. The aggregate annual rent for the leased space is approximately $1.1million.

PART III

Item 10. ***Directors, Executive Officers and Corporate Governance***

The information required by this item with respect to our directors and executive officers will be contained in our 2008 Proxy Statement under the caption "INFORMATION ABOUT OUR DIRECTORS, OFFICERS AND 5% STOCKHOLDERS" and is incorporated in this report by reference.

The information required by this item with respect to Section 16(a) beneficial ownership reporting compliance will be contained in our 2008 Proxy Statement under the caption "Section 16(a) Beneficial Ownership Reporting Compliance" and is incorporated in this report by reference.

The information required by this item with respect to corporate governance matters will be contained in our 2008 Proxy Statement under the caption "Corporate Governance" and is incorporated in this report by reference.

Item 11. ***Executive Compensation***

The information required by this item will be contained in our 2008 Proxy Statement under the captions "DIRECTOR COMPENSATION," "COMPENSATION DISCUSSION AND ANALYSIS" and "EXECUTIVE COMPENSATION" and is incorporated in this report by reference.

Item 12. ***Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters***

The information required by this item with regard to security ownership of certain beneficial owners and management will be contained in our 2008 Proxy Statement under the caption "INFORMATION ABOUT OUR DIRECTORS, OFFICERS AND 5% STOCKHOLDERS—Security Ownership of Certain Beneficial Owners and Management" and is incorporated in this report by reference.

The information required by this item with regard to securities authorized for issuance under equity compensation plans will be contained in our 2008 Proxy Statement under the caption "EXECUTIVE COMPENSATION—Securities Authorized for Issuance under our Equity Compensation Plans" and is incorporated in this report by reference.

Item 13. ***Certain Relationships and Related Transactions, and Director Independence***

The information required by this item will be contained in our 2008 Proxy Statement under the captions "RELATED-PARTY TRANSACTIONS" and "CORPORATE GOVERNANCE" and is incorporated in this report by reference

Item 14. ***Principal Accountant Fees and Services***

The information required by this item will be contained in our 2008 Proxy Statement under the caption "PROPOSAL 3—RATIFICATION OF THE SELECTION OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM" and is incorporated in this report by reference.

PART IV

Item 15. ***Exhibits and Financial Statement Schedules***

(a) 1. *Financial Statements.* The financial statements and notes thereto annexed to this report begin on page F-1.

2. *Financial Statement Schedules.* None

3. *Exhibits.* The Exhibit Index annexed to this report, and immediately preceding the exhibits, is incorporated by reference.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

CYNOSURE, INC.

By: /s/ MICHAEL R. DAVIN
Michael R. Davin
President, Chief Executive Officer and Chairman of the Board of Directors

Pursuant to the requirements of the Securities Act of 1934, this report has been signed by the following persons on behalf of the registrant in the capacities and on the dates indicated.

Signature	Title	Date
/s/ MICHAEL R. DAVIN **Michael R. Davin**	President, Chief Executive Officer and Chairman of the Board of Directors (Principal Executive Officer)	March 13, 2008
/s/ TIMOTHY W. BAKER **Timothy W. Baker**	Executive Vice President and Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer)	March 13, 2008
/s/ ETTORE V. BIAGIONI **Ettore V. Biagioni**	Director	March 13, 2008
/s/ ANDREA CANGIOLI **Andrea Cangioli**	Director	March 13, 2008
/s/ PAUL F. KELLEHER **Paul F. Kelleher**	Director	March 13, 2008
/s/ LEONARDO MASOTTI **Leonardo Masotti**	Director	March 13, 2008
/s/ THOMAS H. ROBINSON **Thomas H. Robinson**	Director	March 13, 2008
/s/ GEORGE J. VOJTA **George J. Vojta**	Director	March 13, 2008

CYNOSURE, INC.

INDEX TO FINANCIAL STATEMENTS

Consolidated Financial Statements of Cynosure, Inc.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders
Cynosure, Inc.:

We have audited the accompanying consolidated balance sheets of Cynosure, Inc. as of December 31, 2007 and 2006, and the related consolidated statements of operations, stockholders' equity and comprehensive income (loss) and cash flows for each of the three years in the period ended December 31, 2007. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Cynosure, Inc. at December 31, 2007 and 2006, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2007, in conformity with U.S. generally accepted accounting principles.

As discussed in Note 2 to the consolidated financial statements, on January 1, 2005, the Company adopted Statement of Financial Accounting Standards No. 123(R), *Share-Based Payment*, using the modified-prospective-transition method.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Cynosure, Inc.'s internal control over financial reporting as of December 31, 2007, based on criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 11, 2008 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Boston, Massachusetts
March 11, 2008

CYNOSURE, INC.

CONSOLIDATED BALANCE SHEETS
(In thousands, except per share data)

	December 31, 2007	December 31, 2006
ASSETS		
Current assets:		
Cash and cash equivalents	$ 39,011	$ 13,690
Marketable securities	47,086	43,556
Accounts receivable, net of allowance of $1,451 and $1,009 in 2007 and 2006, respectively	24,124	19,871
Amounts due from related parties (Note 10)	8	335
Inventories	22,442	17,624
Prepaid expenses and other current assets	4,425	4,977
Deferred income taxes	4,161	2,604
Total current assets	141,257	102,657
Property and equipment, net	7,146	5,662
Other assets	1,441	1,247
Total assets	$149,844	$109,566
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Short-term loan	$ —	$ 167
Accounts payable	2,810	5,986
Amounts due to related party (Note 10)	2,311	1,052
Accrued expenses	17,980	11,077
Deferred revenue	3,939	3,476
Capital lease obligation	485	439
Total current liabilities	27,525	22,197
Capital lease obligation, net of current portion	794	1,069
Deferred revenue, net of current portion	421	311
Other noncurrent liability	226	119
Commitments and Contingencies (Note 16)		
Stockholders' equity:		
Preferred stock, $0.001 par value Authorized—5,000 shares as of December 31, 2007 and 2006 Issued—no shares as of December 31, 2007 and 2006	—	—
Class A and Class B common stock, $0.001 par value Authorized—70,000 shares as of December 31, 2007 and 2006 Issued—12,448 and 11,210 shares as of December 31, 2007 and 2006, respectively	12	11
Additional paid-in capital	101,298	81,026
Retained earnings	20,332	5,820
Accumulated other comprehensive loss	(477)	(700)
Treasury stock, 36 shares, at cost	(287)	(287)
Total stockholders' equity	120,878	85,870
Total liabilities and stockholders' equity	$149,844	$109,566

The accompanying notes are an integral part of these consolidated financial statements.

CYNOSURE, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share data)

	Year Ended December 31,		
	2007	2006	2005
Revenues	$124,315	$78,401	$56,262
Cost of revenues	44,507	32,920	25,843
Gross profit	79,808	45,481	30,419
Operating expenses:			
Sales and marketing	42,058	26,213	17,506
Research and development	6,827	4,673	3,199
General and administrative	11,346	8,975	5,103
Royalty settlement (Note 3)	—	10,000	—
Total operating expenses	60,231	49,861	25,808
Income (loss) from operations	19,577	(4,380)	4,611
Interest income, net	2,516	2,579	89
(Loss) gain on investments (Note 9)	(171)	118	—
Other income (expense), net	866	813	(368)
Income (loss) before provision for (benefit from) income taxes and minority interest	22,788	(870)	4,332
Provision for (benefit from) income taxes	8,276	(266)	102
Minority interest in net income of subsidiary	—	46	70
Net income (loss)	$ 14,512	$ (650)	$ 4,160
Basic net income (loss) per share	$ 1.21	$ (0.06)	$ 0.64
Diluted net income (loss) per share	$ 1.15	$ (0.06)	$ 0.54
Basic weighted average common shares outstanding	11,993	11,084	6,522
Diluted weighted average common shares outstanding	12,654	11,084	7,715

The accompanying notes are an integral part of these consolidated financial statements.

CYNOSURE, INC.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY AND COMPREHENSIVE (LOSS) INCOME
(In thousands)

	Common Stock		Class A and B Common Stock							Treasury Stock			
	Shares	$0.01 Par Value	Shares	$0.001 Par Value	Additional Paid-In Capital	Notes Receivable from Stockholders	Retained Earnings	Deferred Stock-Based Compensation	Accumulated Other Comprehensive (Loss) Income	Shares	Cost	Total Stockholders Equity	Comprehensive Income (Loss)
Balance at December 31, 2004	6,279	$ 63	—	$ —	$12,990	$ (3)	$2,310	$ —	$(433)	(36)	$ (287)	$14,640	$5,302
Sale of common stock	—	—	—	—	—	—	—	—	—	495	1,485	1,485	
Repurchase of common stock	—	—	—	—	—	—	—	—	—	(495)	(1,485)	(1,485)	
Issuance of common stock from public offering, net of offering costs of $2,239	—	—	4,750	5	64,019	—	—	—	—	—	—	64,024	
Conversion of common stock	(6,279)	(63)	6,279	6	57	—	—	—	—	—	—	—	
Issuance of stock options to non-employees	—	—	—	—	205	—	—	—	—	—	—	205	
Deferred stock-based compensation in connection with stock options issued to employees	—	—	—	—	1,690	—	—	(1,690)	—	—	—	—	
Amortization of stock-based compensation	—	—	—	—	—	—	—	264	—	—	—	264	
Repayment of note receivable from stockholders	—	—	—	—	—	3	—	—	—	—	—	3	
Exercise of stock options	—	—	36	—	109	—	—	—	—	—	—	109	
Net income	—	—	—	—	—	—	4,160	—	—	—	—	4,160	$4,160
Cumulative translation adjustment	—	—	—	—	—	—	—	—	(254)	—	—	(254)	(254)
Balance at December 31, 2005	—	—	11,065	11	79,070	—	6,470	(1,426)	(687)	(36)	(287)	83,151	$3,906
Reclassification of deferred compensation	—	—	—	—	(1,426)	—	—	1,426	—	—	—	—	
Stock-based compensation expense	—	—	—	—	2,539	—	—	—	—	—	—	2,539	
Tax benefit from stock-based compensation expense in excess of book deductions	—	—	—	—	397	—	—	—	—	—	—	397	

CYNOSURE, INC.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY AND COMPREHENSIVE (LOSS) INCOME—(Continued)
(In thousands)

	Common Stock		Class A and B Common Stock							Treasury Stock			
	Shares	$0.01 Par Value	Shares	$0.001 Par Value	Additional Paid-In Capital	Notes Receivable from Stockholders	Retained Earnings	Deferred Stock-Based Compensation	Accumulated Other Comprehensive (Loss) Income	Shares	Cost	Total Stockholders Equity	Comprehensive Income (Loss)
Additional IPO costs	—	—	—	—	(38)	—	—	—	—	—	—	(38)	
Exercise of stock options	—	—	145	—	484	—	—	—	—	—	—	484	
Net loss	—	—	—	—	—	—	(650)	—	—	—	—	(650)	$ (650)
Cumulative translation adjustment	—	—	—	—	—	—	—	—	29	—	—	29	29
Unrealized loss on marketable securities, net of tax provision	—	—	—	—	—	—	—	—	(42)	—	—	(42)	(42)
Balance at December 31, 2006	—	—	11,210	11	81,026	—	5,820	—	(700)	(36)	(287)	85,870	$ (663)
Stock-based compensation expense	—	—	—	—	5,777	—	—	—	—	—	—	5,777	
Tax benefit from stock-based compensation expense in excess of book deductions	—	—	—	—	8,434	—	—	—	—	—	—	8,434	
Exercise of stock options	—	—	1,238	1	6,061	—	—	—	—	—	—	6,062	
Net income	—	—	—	—	—	—	14,512	—	—	—	—	14,512	$14,512
Cumulative translation adjustment	—	—	—	—	—	—	—	—	155	—	—	155	155
Unrealized gain on marketable securities, net of tax provision	—	—	—	—	—	—	—	—	68	—	—	68	68
Balance at December 31, 2007	—	$ —	12,448	$12	$101,298	$ —	$20,332	$—	$(477)	(36)	$(287)	$120,878	$14,735

The accompanying notes are an integral part of these consolidated financial statements.

CYNOSURE, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

	Year Ended December 31,		
	2007	2006	2005
Operating activities:			
Net income (loss)	$ 14,512	$ (650)	$ 4,160
Reconciliation of net income (loss) to net cash provided by (used in) operating activities:			
Depreciation and amortization	2,792	2,411	1,769
Loss (gain) on sale of investment	259	(118)	—
Stock-based compensation	5,777	2,474	469
Deferred income taxes	(1,742)	(1,079)	(1,846)
Minority interest in consolidated subsidiary	—	46	22
Accretion of discounts on marketable securities	281	(581)	—
Changes in operating assets and liabilities:			
Accounts receivable	(3,496)	(5,800)	(5,506)
Due from related party	327	(263)	(72)
Inventories	(4,184)	(2,969)	(4,078)
Net book value of demonstration inventory sold	247	177	315
Prepaid expenses and other current assets	1,574	(4,171)	(275)
Accounts payable	(3,261)	2,451	(242)
Due to related party	1,256	78	60
Accrued expenses	6,545	3,872	1,255
Deferred revenue	454	(58)	2,901
Other noncurrent liability	97	77	42
Net cash provided by (used in) operating activities	21,438	(4,103)	(1,026)
Investing activities:			
Purchases of property and equipment	(4,238)	(3,190)	(2,782)
Proceeds from the sales and maturities of securities	68,174	145,894	500
Purchases of marketable securities	(72,140)	(188,561)	—
Acquisition of minority interest	—	(640)	—
Decrease (increase) in other assets	12	(54)	(165)
Net cash (used in) provided by investing activities	(8,192)	(46,551)	(2,447)
Financing activities:			
Payments on short-term loan and note payable to related party	(168)	—	(347)
Tax benefits related to stock options	7,357	397	—
Deposit received for purchase of common stock from investors	—	—	(413)
Deposit paid for repurchase of common stock	—	—	413
Proceeds from sale of common stock and stock option exercises	6,062	484	1,594
Proceeds from initial public offering, net	—	(38)	64,024
Repurchase of common stock	—	—	(1,485)
Payments received on stockholder notes	—	—	3
Payments on capital lease obligation	(440)	(382)	(185)
Net cash provided by financing activities	12,811	461	63,604
Effect of exchange rate changes on cash and cash equivalents	(736)	(763)	487
Net increase (decrease) in cash and cash equivalents	25,321	(50,956)	60,618
Cash and cash equivalents, beginning of year	13,690	64,646	4,028
Cash and cash equivalents, end of year	$ 39,011	$ 13,690	$64,646
Supplemental cash flow information:			
Cash paid for interest	$ 154	$ 131	$ 127
Cash paid for taxes	$ 263	$ 2,898	$ 1,777
Income tax refunds received	$ 1,967	$ —	$ —
Supplemental noncash investing and financing activities:			
Assets acquired under capital lease	$ 204	$ 775	$ 700
Income taxes receivable related to stock options	$ 1,077	$ —	$ —
Deferred compensation associated with stock option grants to employees	$ —	$ —	$ 1,690
Transfer of fixed assets to inventory in connection with October 2005 Sona sale	$ —	$ —	$ 448

The accompanying notes are an integral part of these consolidated financial statements.

1. Nature of the Business

Cynosure, Inc. (Cynosure or the Company) develops, manufactures and markets aesthetic treatment systems that are used by physicians and other practitioners to perform non-invasive or minimally invasive procedures to remove hair, treat vascular lesions, rejuvenate skin through the treatment of shallow vascular lesions and pigmented lesions, temporarily reduce the appearance of cellulite, provide treatments for wrinkles, skin texture and skin discoloration and remove unwanted fat. Cynosure markets and sells its products primarily to the dermatology, plastic surgery and general medical markets, both domestically and internationally. Cynosure is a Delaware corporation, incorporated on July 10, 1991, located in Westford, Massachusetts.

In December 2005, Cynosure completed it's initial public offering (IPO) of class A common stock at a price to the public of $15.00 per share. Cynosure sold 5,750,000 shares of class A common stock, including an over-allotment option of 750,000 shares, and El.En., the selling stockholder in the offering, sold 1,000,000 of the shares. Cynosure received aggregate net proceeds of approximately $64.0 million, after deducting underwriting discounts and commission of approximately $5.0 million and expenses of the offering of approximately $2.3 million. El.En.'s ownership percentage of Cynosure as of December 31, 2007 is 24%.

2. Summary of Significant Accounting Policies

Significant accounting policies followed in the preparation of these consolidated financial statements are as follows:

Management Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and the related disclosures at the date of the financial statements and during the reporting period. Components particularly subject to estimation include the allowance for doubtful accounts, inventory reserves, fair value of stock options and accrued warranties. On an ongoing basis, management evaluates its estimates. Actual results could differ from these estimates.

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of Cynosure, Inc. and its wholly owned subsidiaries: Cynosure GmbH, Cynosure S.A.R.L., Cynosure UK Limited, Cynosure Spain, S.L. and Cynosure KK. In November 2006, Cynosure completed the acquisition of the remaining 48% interest in Suzhou Cynosure Medical Devices, Co. (Suzhou), located in the People's Republic of China and, as a result it is now a wholly owned subsidiary as of December 31, 2006 (See Note 5). All significant intercompany balances and transactions have been eliminated.

Reclassification

Certain amounts in the prior year's financial statements have been reclassified to conform to the current year's presentation, specifically related to the presentation of stock-based compensation expense.

Cash and Cash Equivalents and Marketable Investments

Cynosure considers all short-term, highly liquid investments with original maturities at the time of purchase of 90 days or less to be cash equivalents. Cynosure accounts for investments in marketable securities as available-for-sale securities in accordance with Statement of Financial Accounting Standards (SFAS) No. 115,

Accounting for Certain Investments in Debt and Equity Securities. Under SFAS No. 115, securities purchased to be held for indefinite periods of time and not intended at the time of purchase to be held until maturity are classified as available-for-sale securities. Cynosure continually evaluates whether any marketable investments have been impaired and, if so, whether such impairment is temporary or other than temporary.

Accounts Receivable and Concentration of Credit Risk

Management works to mitigate its concentration of credit risk with respect to accounts receivable through its credit evaluation policies, reasonably short payment terms and geographical dispersion of sales. Revenue includes export sales to foreign companies located principally in Europe, the Asia/Pacific region and the Middle East. Cynosure obtains letters of credit for foreign sales considered by management to be at risk. Cynosure maintains reserves for potential credit losses based upon the aging of its receivable balances, known collectibility issues and its historical experience with losses. In the event that it is determined that the customer may not be able to meet its full obligation to Cynosure, Cynosure records a specific allowance to reduce the related receivable to the amount that Cynosure expects to recover given all information present. No customer accounted for 10% or greater of revenue during 2005, 2006 or 2007. No customer accounted for 10% or greater of accounts receivable as of December 31, 2006 or 2007. Accounts receivable allowance activity consisted of the following for the years ended December 31:

	2007	2006	2005
		(In thousands)	
Balance at beginning of year	$1,009	$ 696	$460
Additions	524	2,289	243
Deductions	(82)	(1,976)	(7)
Balance at end of year	$1,451	$ 1,009	$696

During 2006, Cynosure was notified by Sona MedSpa that it was uncertain that it had the financial resources to honor its commitments to Cynosure under its agreements with Cynosure. In connection with this notification, Cynosure provided an allowance for doubtful accounts totaling approximately $1.5 million for accounts receivable associated with amounts owed by Sona MedSpa. In May 2006, Cynosure sent Sona MedSpa a notice of default with respect to Sona MedSpa's failure to pay Cynosure amounts payable under the agreements between the parties. In June 2006, Cynosure terminated the agreement with Sona MedSpa as the defaults under the agreements were not cured and initiated an arbitration claim pursuant to the terms of the agreement. In November 2006, Cynosure settled its arbitration with Sona MedSpa and released the claims against each other in exchange for consideration of $250,000 in cash. The settlement payment received by Cynosure was recorded within accrued expenses in the accompanying consolidated balance sheet as of December 31, 2006 as this payment was subject to certain avoidance action by a third-party and, if successful, could be subject to forfeiture at that time. As a result of this settlement, Cynosure wrote off approximately $1.9 million in accounts receivable from Sona MedSpa during 2006. In 2007, the period during which this settlement payment was subject to certain avoidance action had lapsed; therefore, the settlement payment, which was in reimbursement for legal expenses, was recorded as a reduction in general and administrative expenses in the accompanying consolidated statements of income for the year ended December 31, 2007.

Inventory

Cynosure states all inventories at the lower of cost or market, determined on a first-in, first-out method. Inventory includes material, labor and overhead and consists of the following:

	December 31,	
	2007	2006
	(In thousands)	
Raw materials	$ 1,467	$ 1,848
Work in process	395	818
Finished goods	20,580	14,958
	$22,442	$17,624

Included in finished goods are lasers used for demonstration purposes. Cynosure's policy is to include demonstration lasers as inventory for a period of up to one year after production at which time the demonstration lasers are either sold or transferred to fixed assets at the lower of cost or market and depreciated over their estimated useful life of three years. Similar to any other finished goods in inventory, Cynosure accounts for such demonstration inventory in accordance with the policy for excess and obsolescence review of Cynosure's entire inventory.

Cynosure's policy is to establish inventory reserves when conditions exist that suggest that inventory may be in excess of anticipated demand or is obsolete based upon assumptions about future demand for products and market conditions. Cynosure regularly evaluates the ability to realize the value of inventory based on a combination of factors including the following: historical usage rates, forecasted sales or usage, product end of life dates, estimated current and future market values and new product introductions. Assumptions used in determining management's estimates of future product demand may prove to be incorrect; in which case the provision required for excess and obsolete inventory would have to be adjusted in the future. If inventory is determined to be overvalued, Cynosure recognizes such costs as cost of goods sold at the time of such determination. Although Cynosure performs a detailed review of its forecasts of future product demand, any significant unanticipated changes in demand could have a significant impact on the value of Cynosure's inventory and reported operating results. Inventory reserve activity consisted of the following for the years ended December 31:

	2007	2006	2005
		(In thousands)	
Balance at beginning of year	$ 995	$1,019	$ 812
Additions	922	624	581
Deductions	(349)	(648)	(374)
Balance at end of year	$1,568	$ 995	$1,019

Cynosure purchases a significant raw material component from one vendor, who is the sole manufacturer of this component. A delay in the production capabilities of this vendor could cause a delay in Cynosure's manufacturing, and a possible loss of revenues, which would adversely affect operating results.

Property and Equipment

Property and equipment are recorded at cost less accumulated depreciation. Depreciation is computed using the straight-line method over the estimated useful lives of the assets. Assets under capital leases and leasehold improvements are amortized using the straight-line method over the shorter of the estimated useful life of the asset or the respective lease term. Included in property and equipment are certain lasers that are used for demonstration purposes, as well as lasers to which Cynosure continues to hold title that are placed at customer locations under a revenue-sharing arrangement. Maintenance and repairs are charged to expense as incurred. Cynosure continually evaluates whether events or circumstances have occurred that indicate that the estimated remaining useful life of its long-lived assets may warrant revision or that the carrying value of these assets may be impaired. Cynosure evaluates the realizability of its long-lived assets based on profitability and cash flow expectations for the related asset. Any write-downs are treated as permanent reductions in the carrying amount of the assets. Based on this evaluation, Cynosure believes that, as of each of the balance sheet dates presented, none of Cynosure's long-lived assets were impaired.

Revenue Recognition and Deferred Revenue

Cynosure generates revenue from the sale of aesthetic treatment systems that are used by physicians and other practitioners to perform various non-invasive and minimally invasive aesthetic procedures. These systems incorporate a broad range of laser and other light-based energy sources. Cynosure offers service and warranty contracts in connection with these sales.

Cynosure recognizes revenue in accordance with Securities and Exchange Commission (SEC) Staff Accounting Bulletin No. 104, *Revenue Recognition in Financial Statements* (SAB 104). Cynosure recognizes revenue from sales of its treatment systems and accessories upon delivery, provided there are no uncertainties regarding customer acceptance, there is persuasive evidence of an arrangement, the fee is fixed or determinable, and collectibility of the related receivable is reasonably assured. Revenues from the sales of service and warranty contracts are deferred and recognized on a straight-line basis over the contract period as services are provided. Payments received by Cynosure in advance of product delivery or performance of services are deferred until earned. Multiple-element arrangements are evaluated in accordance with the principles of Emerging Issues Task Force (EITF) Issue Number 00-21, *Revenue Arrangements with Multiple Deliverables* (EITF 00-21), and Cynosure allocates revenue among the elements based upon each element's relative fair value.

During the year ended December 31, 2006, Cynosure entered into arrangements with two customers that included fees that were not considered to be fixed or determinable. Therefore, revenue was recognized under these arrangements as payments became due. Cynosure recognized $3.0 million and $0.1 million of revenue during the years ended December 31, 2007 and 2006, respectively, under these arrangements.

Cynosure had also entered into a revenue sharing arrangement with Sona MedSpa whereby Cynosure received a percentage of the revenues related to the cosmetic procedures performed at Sona MedSpa locations. Cynosure recognized this revenue in the period the procedure was performed. During the years ended December 31, 2006 and 2005, Cynosure recognized approximately $9,000, and $1,241,000, respectively, under this revenue sharing arrangement. In June 2006, Cynosure terminated this agreement with Sona MedSpa as the defaults under the agreement were not cured.

In accordance with the provisions of EITF Issue Number 00-10, *Accounting for Shipping and Handling Costs* (EITF 00-10), Cynosure records shipping and handling costs billed to its customers as a component of revenue, and the underlying expense as a component of cost of revenue. Shipping and handling costs included as a component of revenue totaled approximately $544,000, $417,000 and $327,000 for the years ended December 31, 2007, 2006 and 2005, respectively. Shipping and handling costs included as a component of cost of revenue totaled $619,000, $478,000 and $445,000 for the years ended December 31, 2007, 2006 and 2005, respectively.

Cynosure collects sales tax from its customers on all product sales for which the customer is not tax exempt and remits such taxes to the appropriate governmental authorities. Cynosure presents its sales taxes on a net basis; therefore, these taxes are excluded from revenues.

Product Warranty Costs

Cynosure typically provides a one-year parts and labor warranty on end-user sales of lasers. Distributor sales generally include a warranty on parts only. Estimated future costs for initial product warranties are provided for at the time of revenue recognition. The following table sets forth activity in the accrued warranty account:

	Years Ended December 31,		
	2007	2006	2005
		(In thousands)	
Balance at beginning of year	$ 2,803	$ 2,265	$ 1,610
Charged to expense	3,821	3,449	2,538
Costs incurred	(3,530)	(2,911)	(1,883)
Balance at end of year	$ 3,094	$ 2,803	$ 2,265

Research and Development

Research and development costs consist of salaries and other personnel-related expenses, including stock-based compensation, of employees primarily engaged in research, development and engineering activities and materials used and other overhead expenses incurred in connection with the design and development of Cynosure's products. These costs are expensed as incurred.

Advertising Costs

Cynosure expenses advertising costs as incurred. Advertising costs totaled $638,000, $550,000 and $405,000 for the years ended December 31, 2006, 2005 and 2004, respectively.

Foreign Currency Translation

The financial statements of Cynosure's foreign subsidiaries are translated from local currency into U.S. dollars using the current exchange rate at the balance sheet date for assets and liabilities, and the average exchange rate prevailing during the period for revenue and expenses. The functional currency for Cynosure's foreign subsidiaries is considered to be the local currency for each entity and, accordingly, translation adjustments for these subsidiaries are included in accumulated other comprehensive income (loss) within stockholders' equity. Certain intercompany and third party foreign currency-denominated transactions generated foreign currency remeasurement gains (losses) of approximately $821,000, $812,000 and ($278,000) during 2007, 2006 and 2005, respectively, which are included in other income (expense), net, in the consolidated statements of operations.

Comprehensive Income (Loss) and Accumulated Other Comprehensive (Loss) Income

Comprehensive income (loss) is the change in equity of a company during a period from transactions and other events and circumstances, excluding transactions resulting from investments by owners and distributions to owners.

The components of accumulated other comprehensive loss as of December 31, 2007 and 2006 are as follows:

	December 31,	
	2007	2006
	(In thousands)	
Unrealized gain (loss) on marketable securities, net of taxes	$ 26	$ (42)
Cumulative translation adjustment	(503)	(658)
Total accumulated other comprehensive loss	$(477)	$(700)

The components of total other comprehensive income (loss) for the years ended December 31, 2007 and 2006 are as follows:

	Years Ended December 31,	
	2007	2006
	(In thousands)	
Cumulative translation adjustment	$155	$ 29
Unrealized gain (loss) on marketable securities:		
Unrealized holding loss on marketable securities	(19)	(42)
Add-back: Reclassification adjustment for impairment of marketable security included in net income	87	—
Gross unrealized gain (loss) on marketable securities	68	(42)
Total other comprehensive income (loss)	$223	$(13)

Fair Value of Financial Instruments

The carrying value of Cynosure's financial instruments, which include cash equivalents, marketable securities, accounts receivable, short-term loan and capital leases, approximates their fair value at December 31, 2007 and 2006.

Stock-Based Compensation

Effective January 1, 2006, Cynosure adopted the fair value recognition provisions of FASB Statement No. 123(R), *Share-Based Payment*, (SFAS 123(R)) using the modified-prospective-transition method. The modified-prospective-transition method is one in which compensation cost is recognized beginning with the effective date (a) for all share-based payments granted after the effective date and (b) for all awards granted to employees prior to the effective date of SFAS 123(R) that remain unvested on the effective date. In addition, SFAS 123(R) requires companies to utilize an estimated forfeiture rate when calculating the expense for the period, whereas, SFAS 123 permitted companies to record forfeitures based on actual forfeitures, which was Cynosure's historical policy under SFAS 123.

During the year ended December 31, 2006, Cynosure applied an estimated annual forfeiture rate of 1% in determining the expense recorded in the consolidated statements of income. Upon review of its actual rate of forfeitures since the adoption of SFAS 123(R) and in consideration of management's expectations for future forfeitures, Cynosure changed its estimated annual forfeiture rate in 2007 from 1% to 5%. This change in estimate was applied retrospectively and Cynosure recorded a cumulative catch-up adjustment of approximately $313,000 as a reduction in stock-based compensation expense during the year ended December 31, 2007.

Cynosure recorded stock-based compensation expense of $5.8 million and $2.5 million and related tax benefits of $1.8 million and $652,000 for the years ended December 31, 2007 and 2006, respectively. Additionally, as a result of implementation of SFAS 123(R), as of January 1, 2006, Cynosure reversed approximately $1.4 million of remaining deferred stock-based compensation associated with the May 2005 option grants. Cynosure capitalized $65,000 of stock-based compensation expense as a part of inventory as of December 31, 2007 and 2006.

Total stock-based compensation expense was recorded to cost of revenues and operating expenses based upon the functional responsibilities of the individual holding the respective options, as follows:

	Years Ended December 31,	
	2007	2006
	(In thousands)	
Cost of revenues	$ 373	$ 82
Sales and marketing	1,966	695
Research and development	1,410	652
General and administrative	2,028	1,045
Total stock-based compensation expense	$5,777	$2,474

As of December 31, 2007, there was $12.5 million of unrecognized compensation expense related to non-vested share awards that is expected to be recognized on a straight-line basis over a weighted-average period of 2.1 years. Cash received from option exercises was $6.1 million and $484,000 during the years ended December 31, 2007 and 2006, respectively. Cynosure recognized $8.4 million and $397,000 in tax benefits in excess of book deductions from these option exercises during the years ended December 31, 2007 and 2006, respectively.

Cynosure granted 588,050 and 522,150 stock options during the years ended December 31, 2007 and 2006, respectively. Effective with the adoption of SFAS 123(R), Cynosure uses the Black-Scholes option pricing model to determine the weighted average fair value of options, rather than a binomial model. The weighted-average fair value of the options granted during the years ended December 31, 2007 and 2006 was $18.84 and $11.52 using the following assumptions:

	Years Ended December 31,	
	2007	2006
Risk-free interest rate	3.35% - 4.77%	3.88% - 5.00%
Expected dividend yield	—	—
Expected term	5.8 years	5.8 years
Expected volatility	70%	77% - 82%

Option-pricing models require the input of various subjective assumptions, including the option's expected life and the price volatility of the underlying stock. Due to Cynosure's initial public offering in December 2005, Cynosure believes there is not adequate information on the volatility of its own shares. As such, Cynosure's estimated expected stock price volatility is based on a weighted-average of its own historic volatility and of the average volatilities of other similar companies in the same industry. Cynosure believes this is more reflective and a better indicator of the expected future volatility, than using an average of a comparable market index or of a single comparable company in the same industry. Cynosure's expected term of options granted during the twelve months ended December 31, 2007 and 2006 was derived from the short-cut method described in SEC's Staff Accounting Bulletin (SAB) No. 107. The risk-free rate for the expected term of the option is based on the U.S. Treasury yield curve in effect at the time of grant. The dividend yield of zero is based on the fact that Cynosure has never paid cash dividends and has no present intention to pay cash dividends.

Cynosure accounts for transactions in which services are received from non-employees in exchange for equity instruments based on the fair value of such services received or of the equity instruments issued, whichever is more reliably measured, in accordance with SFAS No. 123(R) and the Emerging Issues Task Force Issue No. 96-18, *Accounting for Equity Instruments that are Issued to Other than Employees for Acquiring, or in Conjunction with Selling, Goods or Services*, or EITF Issue No. 96-18.

In July 2006, Cynosure entered into a consulting agreement with a former employee, who agreed to provide services to the Company after his employment terminates for a period of one year from the effective date of the agreement. This consulting agreement can be terminated at any time by either party. In connection with this agreement, all vested incentive stock options granted to this former employee were converted into an equivalent number of vested non-qualified stock options in order to avoid termination of such options and allow the former employee to exercise such options during the term of the consulting agreement. This agreement also provided for an additional year of vesting of all of the unvested options previously granted to the former employee, while he was employed by the Company, throughout the term of the consulting agreement. During the years ended December 31, 2007 and 2006, Cynosure recorded approximately $660,000 and $363,000 of additional stock-based compensation expense related to this agreement.

Prior to January 1, 2006, Cynosure accounted for stock-based awards under the recognition and measurement provisions of Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees*, and related Interpretations, as permitted by Financial Accounting Standards Board (FASB) Statement No. 123, *Accounting for Stock-Based Compensation* (SFAS 123). In accordance with the modified-prospective-transition method of SFAS 123(R), Cynosure has not restated results for prior periods. Under the intrinsic-value method, compensation expense is measured on the date of grant as the difference between the deemed fair market value of Cynosure's common stock for accounting purposes and the option exercise price multiplied by the number of options granted. Generally, Cynosure granted stock options with exercise prices equal to the fair market value for accounting purposes of its common stock; however, to the extent that the deemed fair market value for accounting purposes of the common stock exceeded the exercise price, Cynosure recorded deferred

stock-based compensation and amortized the expense over the vesting schedule of the options, generally four years. The fair value for accounting purposes of Cynosure's common stock was determined by the Company's board of directors. Prior to the completion of the Cynosure's IPO, Cynosure's board of directors considered objective and subjective factors in determining the fair value of Cynosure's common stock for accounting purposes. During the year ended December 31, 2005, Cynosure granted stock options with exercise prices less than the deemed fair market value of common stock for accounting purposes and, as a result, recorded deferred stock-based compensation of approximately $1.7 million. During the year ended December 31, 2005, Cynosure recorded amortization of deferred stock-based compensation of $264,000.

If compensation cost had been determined for stock options granted to employees based on the fair value of the awards at the date of grant in accordance with the provisions of SFAS 123, Cynosure's net income would have been the pro forma amount indicated below:

	Year Ended December 31, 2005 (In thousands, except per share data)
Net income:	
As reported	$4,160
Add: Stock-based employee compensation expense included in determination of net income, net of tax	171
Less: Total stock-based employee compensation expense determined under the fair value-based method, net of tax	(636)
Pro forma net income:	$3,695
Basic net income per share—as reported	$ 0.64
Diluted net income per share—as reported	$ 0.54
Basic net income per share—pro forma	$ 0.57
Diluted net income per share—pro forma	$ 0.48

In computing this pro forma amount, the Company used the Black-Scholes pricing model using the following assumptions for options granted in fiscal year 2005:

	Year Ended December 31, 2005
Risk-free interest rate	3.88%
Expected dividend yield	—
Expected lives	5 years
Expected volatility	75%
Weighted average fair value	$7.06

Income Taxes

Cynosure provides for income taxes in accordance with SFAS No. 109, *Accounting for Income Taxes* (SFAS 109). SFAS 109 recognizes tax assets and liabilities for the cumulative effect of all temporary differences between the financial statement carrying amounts and the tax basis of assets and liabilities, and are measured using the enacted tax rates that will be in effect when these differences are expected to reverse. Valuation allowances are provided if, based on the weight of available evidence, it is more likely than not that some or all of the deferred tax assets will not be realized.

Cynosure adopted the provisions of FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes, an Interpretation of FAS 109, Accounting for Income Taxes*, (FIN 48) on January 1, 2007. FIN 48 clarifies the accounting for income taxes, by prescribing a minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. FIN 48 also provides guidance on derecognition, measurement, classification, interest and penalties, accounting in interim periods, disclosure and transition. The adoption of FIN 48 did not have a material impact to Cynosure.

Net Income (Loss) per Common Share

Basic net income (loss) per share is determined by dividing net income (loss) by the weighted average common shares outstanding during the period. Diluted net income per share is determined by dividing net income by the diluted weighted average shares outstanding during the period. Diluted weighted average shares reflect the dilutive effect, if any, of common stock options based on the treasury stock method.

The reconciliation of basic and diluted weighted average shares outstanding for the years ended December 31, 2007 and 2005 is as follows:

	Years Ended December 31,	
	2007	2005
Basic weighted average common shares outstanding	11,993	6,522
Weighted average common equivalent shares	661	1,193
Diluted weighted average common shares outstanding	12,654	7,715

For the year ended December 31, 2007, options to purchase approximately 249,000 were excluded from the calculation of diluted weighted average common shares outstanding as their effect was antidilutive. There were no antidilutive shares for the year ended December 31, 2005.

For the year ended December 31, 2006, the number of basic and diluted weighted average shares outstanding were the same. The Company had outstanding options to purchase approximately 2.2 million shares of the Company's common stock that were potential dilutive securities outstanding as of December 31, 2006; however, any increase in the number of shares of common stock equivalents for the year ended December 31, 2006 would be antidilutive based on the net loss for that year and therefore were not included.

Recent Accounting Pronouncements

In September 2006, the FASB issued Statement No. 157, *Fair Value Measurements*, (SFAS 157). SFAS 157 defines fair value, establishes a framework for measuring fair value in accordance with generally accepted accounting principles, and expands disclosures about fair value measurements. This Statement does not require any new fair value measurements; rather, it applies under other accounting pronouncements that require or permit fair value measurements. The provisions of this Statement are to be applied prospectively as of January 1, 2008, with any transition adjustment recognized as a cumulative-effect adjustment to the opening balance of retained earnings. Cynosure does not expect that the adoption of SFAS 157 will have a material impact on its financial position or results of operations.

In February 2007, the FASB issued Statement No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities—Including an Amendment of FASB Statement No. 115* (SFAS 159), in order to permit entities to choose to measure many financial instruments and certain other eligible items at fair value at specified election dates and, thereby, mitigate volatility in reported earnings caused by measuring related assets and liabilities differently. Unrealized gains and losses on items for which the fair value option has been elected shall be reported in earnings. The provisions of SFAS 159 are to be applied prospectively as of January 1, 2008;

however early adoption is permitted, subject to certain restrictions, as defined. SFAS 159 does not affect any existing accounting literature that requires certain assets and liabilities to be carried at fair value. Cynosure does not expect that the adoption of SFAS 159 will have a material impact on its financial position or results of operations.

In December 2007, the FASB issued Statement No. 141(R), *Applying the Acquisition Method* (SFAS 141(R)), which replaces FASB Statement No. 141, *Business Combinations*. This Statement retains the fundamental requirements in Statement 141 that the acquisition method of accounting (which Statement 141 called the purchase method) be used for all business combinations and for an acquirer to be identified for each business combination. This Statement defines the acquirer as the entity that obtains control of one or more businesses in the business combination and establishes the acquisition date as the date that the acquirer achieves control. Statement 141 did not define the acquirer, although it included guidance on identifying the acquirer, as does this Statement. This Statement's scope is broader than that of Statement 141, which applied only to business combinations in which control was obtained by transferring consideration. By applying the same method of accounting—the acquisition method—to all transactions and other events in which one entity obtains control over one or more other businesses, this Statement improves the comparability of the information about business combinations provided in financial reports. SFAS 141(R) applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. Cynosure does not expect that the adoption of SFAS 141(R) will have a material impact on its financial position or results of operations.

In December 2007, the FASB issued Statement No. 160, *Noncontrolling Interests in Consolidated Financial Statements—an amendment of ARB No. 51* (SFAS 160), which applies to all entities that prepare consolidated financial statements, except not-for-profit organizations, but will affect only those entities that have an outstanding noncontrolling interest in one or more subsidiaries or that deconsolidate a subsidiary. This Statement amends ARB 51 to establish accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. It clarifies that a noncontrolling interest in a subsidiary is an ownership interest in the consolidated entity that should be reported as equity in the consolidated financial statements. SFAS 160 is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008. Earlier adoption is prohibited. SFAS 160 shall be applied prospectively as of the beginning of the fiscal year in which this Statement is initially applied, except for the presentation and disclosure requirements. The presentation and disclosure requirements shall be applied retrospectively for all periods presented. Cynosure does not expect that the adoption of SFAS 160 will have a material impact on its financial position or results of operations.

3. Royalty Settlement

In the third quarter of 2006, Cynosure entered into negotiations with Palomar with respect to such a license. On November 6, 2006, Cynosure entered into a non-exclusive patent license with Palomar. Under the cross-license agreement, Cynosure obtained a non-exclusive license to integrate into its products certain hair removal technology covered by specified U.S. and foreign patents held by Palomar and Palomar obtained a non-exclusive license under certain U.S. and foreign patents held by Cynosure. In November 2006, Cynosure made a payment to Palomar of $10 million for royalties related to sales prior to October 1, 2006 of hair removal-only systems including Cynosure's Apogee family of products, *PhotoLight*, *Acclaim 7000* and the *PhotoSilk Plus*. Cynosure recorded this amount as a royalty settlement within Cynosure's operating expenses for the year ended December 31, 2006.

In connection with this agreement, Cynosure also agreed to pay royalties to Palomar on Cynosure's future sales of certain hair removal products. The royalty rate for future sales of hair removal products ranges from 3.75% to 7.5% of net sales beginning October 1, 2006, depending upon product configuration and the number of energy sources. Royalty expense associated with such sales is recorded as cost of revenues. Cynosure's revenue from systems that do not include hair removal capabilities and revenue from service is not subject to any past or future royalties under the Palomar agreement.

4. Marketable Securities

Cynosure's available-for-sale securities at December 31, 2007 consist of approximately $47.1 million of investments in debt securities consisting of state and municipal bonds and approximately $10,000 in equity securities. As of December 31, 2007, Cynosure's equity securities consist of 133,511 shares of common stock of a public company with a fair market value of approximately $10,000. These shares were acquired in connection with the sale of Cynosure's investment in a private company during the year ended December 31, 2006 and are considered available-for-sale securities in accordance with SFAS No. 115. (See Note 9 for further discussion.) All investments are recorded at fair market value, with any unrealized gains and losses reported as a separate component of accumulated other comprehensive loss.

As of December 31, 2007, Cynosure's marketable securities consist of the following (in thousands):

	Market Value	Amortized Cost	Unrealized Gains	Unrealized Losses
State and municipal bonds	$47,076	$47,037	$ 39	$ —
Equity security	10	10	—	—
	$47,086	$47,047	$ 39	$ —

During the year ended December 31, 2007, Cynosure concluded that its equity security investment in shares of common stock of another public company was other than temporarily impaired as of December 31, 2007 due to its consistent decline in value and public notification that the security is at risk of being delisted from the NASDAQ exchange. As such, Cynosure recorded an other than temporary impairment charge of approximately $235,000 on the investment, which is included in the consolidated statement of operations, for the year ended December 31, 2007.

As of December 31, 2007, Cynosure's investments in debt securities mature as follows (in thousands):

		Maturities	
	Total	Less Than One Year	One to Two Years
State and municipal bonds	$47,076	$44,481	$2,595

Cynosure's marketable securities portfolio includes Auction Rate Securities ("ARS") of $29.3 million from various issuers collateralized by student loans and municipal debt. ARSs are securities with long-term contractual maturities but with interest rates that are reset every seven to 35 days by auctions. At the end of each reset period, investors can sell or continue to hold the securities at par. On February 13, 2008, certain ARSs that Cynosure held experienced failed auctions that limited the liquidity of these securities. Based on current market conditions, it is likely that auction failures will continue that could result in either temporary or other-than-temporary impairments of our ARS holdings. Cynosure has the ability and intent to hold these securities until a successful auction occurs and the ARSs are liquidated at par value. If in the future Cynosure determines that any decline in value of the ARSs is other-than-temporary, Cynosure would be required to recognize the loss in our statement of operations, which could have a material impact on Cynosure's operating results in the period it is recognized. Further, as the funds associated with the ARSs may not be accessible for longer than twelve months because of continued failed auctions or Cynosure's inability to find a buyer outside of the auction process, Cynosure may classify these securities as long-term assets in Cynosure's consolidated balance sheet as of March 31, 2008, or thereafter.

5. Acquisition of Minority Interest

On August 31, 2006, Cynosure acquired the remaining 48% minority interest in Suzhou Cynosure Medical Devices Company, Ltd.'s (Suzhou) outstanding common stock for a purchase price of $640,000 in cash. Cynosure did not incur any material closing costs related to the purchase and, as such, the $640,000 cash consideration represents the entire purchase price. The business purpose of acquiring the minority interest was to gain complete control over Suzhou while extending the business license of Suzhou. The purchase of the minority interest was contingent upon Chinese government approval of the shareholder transfer from the seller to Cynosure for the shares acquired and approval of extension of the business license of Suzhou for a period of 20 years. The existing business license was set to expire on October 12, 2007. On November 10, 2006, Suzhou received such approval from the Chinese government, evidenced by the issuance of a new business license allowing operations in China until October 12, 2027.

In accordance with SFAS No. 141, *Business Combinations,* the acquisition of the minority interest was accounted for as a business combination, which required allocation of the purchase price to assets acquired and liabilities assumed. As such, the aggregate purchase price of $640,000 was allocated to the net assets acquired from the minority interest holders of Suzhou, which had a total value of $357,000 and consisted primarily of $263,000 of cash, $148,000 of accounts receivable, $487,000 of inventory, $36,000 of other assets, and $190,000 of other current liabilities as of August 31, 2006, with the residual of $283,000 allocated to the business license, which is subject to amortization due to its limited useful life. This acquired intangible asset is included in other assets in the accompanying consolidated balance sheet as of December 31, 2006 and is being amortized on a straight-line basis over a 20-year period, which approximates the expected cash flows resulting from the underlying asset.

6. Segment and Geographic Information

In accordance with SFAS No. 131, *Disclosures about Segments of an Enterprise and Related Information* (SFAS 131), operating segments are identified as components of an enterprise about which separate discrete financial information is available for evaluation by the chief operating decision maker, or decision-making group, in making decisions how to allocate resources and assess performance. Cynosure's chief decision-maker, as defined under SFAS 131, is a combination of the Chief Executive Officer and the Chief Financial Officer. Cynosure views its operations and manages its business as one segment, aesthetic treatment products and services.

The following table represents total revenue by geographic destination:

	Year Ended December 31,		
	2007	2006	2005
		(In thousands)	
United States	$ 71,605	$39,670	$28,867
Europe	27,373	20,011	12,725
Asia/Pacific	12,970	10,356	7,059
Other	12,367	8,364	7,611
	$124,315	$78,401	$56,262

Net assets by geographic area are as follows:

	December 31,	
	2007	2006
	(In thousands)	
United States	$118,074	$86,815
Europe	6,116	443
Asia/Pacific	837	374
Eliminations	(4,149)	(1,762)
	$120,878	$85,870

Long-lived assets by geographic area are as follows:

	December 31,	
	2007	2006
	(In thousands)	
United States	$7,829	$6,435
Europe	589	316
Asia/Pacific	169	157
Eliminations	—	—
	$8,587	$6,909

No individual country within Europe or Asia/Pacific represented greater than 10% of total revenue or net assets for any period presented.

7. Balance Sheet Accounts

Property and Equipment

Property and equipment consists of the following at December 31:

	Estimated Useful Life (Years)	2007 Cost	2006 Cost
		(In thousands)	
Equipment	3-5	$ 2,857	$ 2,578
Furniture and fixtures	5	1,007	748
Computer equipment and software	3	1,997	1,724
Leasehold improvements	5	812	724
Demonstration equipment	3	10,422	7,737
Revenue sharing lasers	3	235	233
Construction in-progress		524	—
		17,854	13,744
Less: Accumulated depreciation and amortization		(10,708)	(8,082)
		$ 7,146	$ 5,662

Construction in-progress primarily relates to Cynosure's software development costs that are being capitalized in accordance with AICPA's Statement of Position (SOP) 98-1, *Accounting for the Costs of Computer Software Developed or Obtained for Internal Use.*

Depreciation expense relating to property and equipment was $2,730,000, $2,341,000 and $1,733,000 for the years ended December 31, 2007, 2006 and 2005, respectively. As of December 31, 2007 and 2006, the cost of assets recorded under capitalized leases was approximately $2,772,000 and $2,472,000, and the related accumulated amortization was approximately $1,442,000 and $993,000, respectively. Amortization expense of assets recorded under capitalized leases is included as a component of depreciation expense.

Accrued Expenses

Accrued expenses consist of the following at December 31:

	2007	2006
	(In thousands)	
Accrued payroll and taxes	$ 2,991	$ 1,565
Accrued employee benefits	432	427
Accrued warranty costs	3,392	2,803
Accrued commissions	3,534	1,761
Accrued legal fees	126	117
Accrued income tax	2,718	797
Accrued other	4,787	3,607
	$17,980	$11,077

8. Investment in Sona MedSpa

In 2001, Cynosure invested $1,500,000 in the Series A preferred stock of Sona MedSpa International, Inc. (Sona MedSpa), a spa franchise or that owns and operates hair removal clinics in the United States. Cynosure's equity investment represented a 40% equity ownership of Sona MedSpa, which Cynosure accounted for under the equity method of accounting, which required classification of Sona MedSpa as a related party. During 2000 and 2001, Cynosure agreed to guarantee certain Sona MedSpa lease commitments (see Note 16). The Company recognized $154,000 as the Company's share of Sona MedSpa's (loss) income as a component of other (expense) income for the year ended December 31, 2004. In May 2004, Cynosure sold its 40% equity interest in Sona MedSpa for $3.6 million, resulting in a $3.0 million gain. Of the sales price, $2.6 million was received in cash and $1.0 million was deposited in escrow to be received in three installments over the next 18 months. As of December 31, 2005, all amounts deposited in escrow were released to Cynosure.

In connection with the original investment in Sona MedSpa, Cynosure also entered into a revenue sharing arrangement with Sona MedSpa whereby Cynosure provided lasers to Sona MedSpa and, in return, received a percentage of the revenues related to the aesthetic procedures performed at Sona MedSpa locations. Simultaneous with the sale of Cynosure's equity investment, Cynosure sold certain lasers previously placed in Sona MedSpa clinics to Sona MedSpa for $1.2 million, which is included in Cynosure revenues in 2004. Cynosure also entered into an amended laser placement and revenue sharing arrangement with the new owners of Sona MedSpa. Effective May 24, 2004, Cynosure had no ongoing ownership interest in Sona MedSpa and Sona MedSpa was no longer considered a related party. During the years ended December 31, 2005 and 2004, Cynosure recognized approximately $1,241,000 and $2,402,000, respectively, under the revenue sharing arrangement of which $1,269,000 is presented as related party revenues in the accompanying consolidated statement of operations for the year ended December 31, 2004, prior to the sale of the equity interest.

In October 2005, Cynosure entered into a preferred vendor agreement with Sona MedSpa whereby Cynosure sold certain laser systems to Sona Medspa for approximately $1.3 million, which was recorded as deferred revenue as of December 31, 2005 because the fee was not fixed or determinable at the time of sale.

In March 2006, Sona MedSpa notified Cynosure that Sona MedSpa was uncertain that it had the financial resources to honor its commitments to Cynosure and Cynosure determined that the collectibility of the fee was not probable and, as a result, reversed the related deferred revenue. Cynosure expensed as cost of goods sold approximately $667,000 of inventory delivered under the agreement. Additionally, Cynosure provided an allowance for doubtful accounts of $463,000 for accounts receivable associated with services provided prior to the October 2005 preferred vendor agreement. On May 2, 2006, Cynosure sent Sona MedSpa a notice of default with respect to Sona MedSpa's failure to pay Cynosure amounts payable under two agreements between the parties. On June 2, 2006, Cynosure terminated the agreement with Sona MedSpa as the defaults under the agreements were not cured.

On November 27, 2006, Cynosure settled its arbitration with Sona MedSpa and released the claims against each other in exchange for consideration of $250,000 in cash. The settlement payment received by Cynosure has been recorded within accrued expenses in the accompanying consolidated balance sheet as of December 31, 2006 as this payment may be subject to certain avoidance action by a third-party and, if successful, could be subject to forfeiture. In 2007, the period during which this settlement payment was subject to certain avoidance action had lapsed; therefore, the settlement payment, which was in reimbursement for legal expenses, was recorded as a reduction in general and administrative expenses in the accompanying consolidated statements of income for the year ended December 31, 2007.

9. Investment in OccuLogix, Inc.

During 2003, Cynosure made an investment in Solx, Inc., a private company that represents an approximate 2% ownership interest in the entity. During the year ended December 31, 2005, Cynosure recognized revenue of approximately $365,000, related to laser sales to this entity and did not recognize any revenue to this entity during the year ended December 31, 2006.

In August 2006, Cynosure sold its investment interest to OccuLogix, Inc., a public company, in exchange for consideration consisting of (1) approximately $379,000 in cash, and (2) 133,511 shares of common stock of the acquiring company with a fair market value of approximately $270,000 at the time of the sale. As a result of this sale, during the year ended December 31, 2006, Cynosure received approximately $105,000 in cash and recorded a gain of approximately $118,000, which is included in gain on sale of investment in the accompanying consolidated statements of operations. The remaining cash consideration of approximately $274,000 is to be paid in the following installments: $64,000 in August 2007, $105,000 in August 2008 and $105,000 upon the achievement of a certain contingent event, as specified in the transaction agreement. During the year ended December 31, 2007, Cynosure received the August 2007 payment of $64,000 in cash and recorded this as gain on sale of investment in the consolidated statements of operations. Due to collection based on a contingent event and uncertainty regarding collection of the August 2008 payment, Cynosure deferred the gain related to the remaining cash consideration of $210,000 and will record this as a gain if and when it receives the remaining cash payments.

The value of the shares of the acquiring company's common stock is included in Cynosure's marketable securities on the accompanying consolidated balance sheet as they are considered available-for-sale securities in accordance with SFAS No. 115. During the year ended December 31, 2007, Cynosure concluded that the value of these shares was other than temporarily impaired as of December 31, 2007 due to its consistent decline in value and public notification that the security is at risk of being delisted from the NASDAQ exchange. As such, Cynosure recorded an impairment charge of approximately $235,000, net of related taxes, as an other than temporary impairment on the investment in the accompanying consolidated statements of operations for the year ended December 31, 2007.

10. Related Party Transactions

Purchases of inventory from El.En. during the years ended December 31, 2007, 2006 and 2005 were approximately $8,131,000, $3,222,000 and $2,423,000, respectively. As of December 31, 2007 and 2006, amounts due to related party for these purchases were approximately $2.3 million and $1.1 million, respectively. Amounts due from El.En. as of December 31, 2007 and 2006 were $8,000 and $335,000, respectively, which represent services performed by Cynosure.

11. Short-term Loan

Cynosure's short-term loan consists of a line of credit with a bank which expired on May 11, 2007 and bears interest at 5.11%. There were no amounts available for borrowing at December 31, 2006 and the note was fully paid during the year ended December 31, 2007.

12. Stockholders' Equity

Common Stock Authorized

In connection with the Cynosure IPO in December 2005, Cynosure restated it's certificate of incorporation to create a dual class capital structure by authorizing $0.001 par value class A and class B common stock and reclassifying all of Cynosure's shares of previously existing $0.01 par value common stock into shares of class B common stock. In addition, each outstanding option to purchase shares of common stock automatically became an option to purchase an equal number of shares of our class B common stock, with no other changes to the term of the option. Cynosure has authorized 61,500,000 shares of $0.001 par value class A common stock and 8,500,000 shares of $0.001 par value class B common stock. As of December 31, 2007, there were 9,473,487 shares of class A common stock issued and 2,975,297 shares of class B common stock issued.

The rights, preferences and privileges of each class of common stock are as follows:

Voting Rights

The holders of class A common stock and class B common stock have identical rights and will be entitled to one vote per share with respect to each matter presented to Cynosure stockholders on which the holders of common stock are entitled to vote, except for the approval rights of the holders of the class B common stock applicable to specified amendments to Cynosure's certificate of incorporation and amendments of Cynosure's bylaws by stockholders and except with respect to the election and removal of directors. El.En., Cynosure's largest stockholder, is able to control the election of a majority of the members of Cynosure's board of directors. El.En. owns 95% of Cynosure's outstanding class B common stock, which comprises 35% of Cynosure's aggregate outstanding common stock. Until El.En. beneficially owns less than 20% of the aggregate number of shares of Cynosure's class A common stock and class B common stock outstanding or less than 50% of the number of shares of Cynosure's class B common stock outstanding, El.En., as holder of a majority of the shares of Cynosure's class B common stock, will have the right:

- to elect a majority of the members of Cynosure's board of directors;
- to approve amendments to our bylaws adopted by Cynosure's class A and class B stockholders, voting as a single class; and
- to approve amendments to any provisions of Cynosure's restated certificate of incorporation relating to the rights of holders of common stock, the powers, election and classification of the board of directors, corporate opportunities and the rights of holders of class A common stock and class B common stock to elect and remove directors, act by written consent and call special meetings of stockholders.

In addition, the holders of shares of Cynosure's class B common stock will vote with Cynosure's class A stockholders for the election of the remaining directors.

Conversion

Cynosure's class A common stock is not convertible into any other shares of Cynosure's capital stock.

Each share of class B common stock is convertible into one share of class A common stock at any time at the option of the holder. In addition, each share of class B common stock shall convert automatically into one share of class A common stock upon any transfer of such share of class B common stock, whether or not for value.

Dividends

Subject to preferences that may apply to any shares of preferred stock outstanding at the time, the holders of class A common stock and class B common stock shall be entitled to share equally, on a per share basis, in any dividends that Cynosure's board of directors may determine to issue from time to time.

Liquidation Rights

In the event of our liquidation or dissolution, the holders of class A common stock and class B common stock shall be entitled to share equally, on a per share basis, in all assets remaining after the payment of all debts and other liabilities and subject to the prior rights of any outstanding preferred stock.

Issuances of Common Stock

In December 2005, Cynosure completed its IPO of 4,000,000 shares of common stock at $15.00 per share and sold an additional 750,000 shares of common stock at $15.00 per share as a result of the exercise of the over-allotment option by the underwriters of the IPO. The sale of the 4,750,000 shares of common stock in connection with the IPO resulted in net proceeds to Cynosure of approximately $64,024,000, after deducting underwriting discounts and offering-related expenses.

During October and November 2004, Cynosure entered into Stock Subscription Agreements (the Agreements) with certain accredited investors for the purchase of 575,000 shares of Cynosure common stock at $3.00 per share. The purchase price was payable in two installments, 50% upon execution of the subscription agreement and 50% due April 1, 2005. Certain of the subscription agreements required a single payment due April 15, 2005. The common stock sold under the Agreements was issued in April 2005.

In connection with the signing of the stock subscription agreements, Cynosure entered into a Stock Purchase Agreement with El.En. to purchase 575,000 shares of Cynosure common stock at $3.00 per share to be delivered to the accredited investors pursuant to the subscription agreements. The payment terms of the Stock Purchase Agreement mirrored those of the subscription agreement. The common stock was purchased in April 2005 and recorded as a reduction of additional paid-in capital.

Preferred Stock

Cynosure has authorized 5,000,000 shares of $0.001 par value preferred stock. The Board of Directors has full authority to issue this stock and to fix the voting powers, preference rights, qualifications, limitations, or restrictions thereof, including dividend rights, conversion rights, redemption privileges and liquidation preferences and the number of shares constituting any series or designation of such series.

13. Stock-Based Compensation

1992 Stock Option Plan

In February 1992, the Board of Directors adopted, and the stockholders approved, the 1992 Stock Option Plan (the 1992 Plan). The 1992 Plan provided for the grant of incentive stock options (ISOs), as well as nonstatutory options. The Board of Directors administered the 1992 Plan and had sole discretion to grant options to purchase shares of the Company's common stock.

The Board of Directors determined the term of each option, option price, number of shares for which each option was granted, whether restrictions would be imposed on the shares subject to options and the rate at which each option was exercisable. The exercise price for options granted was determined by the Board of Directors, except that for ISOs, the exercise price could not be less than the fair market value per share of the underlying common stock on the date granted (110% of fair market value for ISOs granted to holders of more than 10% of the voting stock of the Cynosure). The term of the options were set forth in the applicable option agreements, except that in the case of ISOs, the option term was not to exceed ten years (five years for ISOs granted to holders of more than 10% of voting stock of the Cynosure). A maximum of 2,250,000 shares of common stock

were reserved for issuance in accordance with the 1992 Plan. Options granted under the 1992 Plan vested either (i) over a 50-month period at the rate of 24% after the first year and 2% each month thereafter until fully vested or (ii) after eight years with acceleration of vesting if certain performance measures were met, as defined in the agreements. All options granted under the 1992 Plan to date were issued at fair market value as determined by the Board of Directors. The 1992 Plan expired on the tenth anniversary of the date of its adoption by the Board of Directors in February 2002. Options outstanding as of this date continue to have force and effect in accordance with the provisions of the instruments evidencing such options.

2004 Stock Option Plan

In October 2004, the Board of Directors adopted and the stockholders approved the 2004 Stock Option Plan (the 2004 Plan). The 2004 Plan provided for the grant of ISOs, as well as nonstatutory options. The Board of Directors administers the 2004 Plan and had sole discretion to grant options to purchase shares of Cynosure's common stock.

The Board of Directors determines the term of each option, option price, number of shares for which each option is granted, whether restrictions would be imposed on the shares subject to options and the rate at which each option is exercisable. The exercise price for options granted is determined by the Board of Directors, except that for ISOs, the exercise price could not be less than the fair market value per share of the underlying common stock on the date granted (110% of fair market value for ISOs granted to holders of more than 10% of the voting stock of Cynosure). The term of the options is set forth in the applicable option agreement, except that in the case of ISOs, the option term cannot exceed ten years. Options granted under the Plan vested either (i) over a 48-month period at the rate of 25% after the first year and 6.25% each quarter thereafter until fully vested or (ii) over a vesting period determined by the Board of Directors. As of December 31, 2007, there are no shares available for future grant under the 2004 Plan.

In April and May 2005, Cynosure granted 10,000 and 358,200 options, respectively, to purchase common stock under the 2004 Plan. At the time of grant, these options were believed to have been issued at fair market value. Subsequently, the Board of Directors determined the April and May 2005 option grants were issued below the deemed fair market value for accounting purposes as supported by a retrospective valuation conducted by Cynosure and recorded approximately $1.7 million of deferred stock-based compensation expense which is being amortized over the vesting period of the options. During the year ended December 31, 2005, Cynosure recorded amortization of deferred stock-based compensation of $264,000. As a result of the implementation of SFAS 123(R), as of January 1, 2006, the Company reversed approximately $1.4 million of the remaining deferred stock-based compensation.

In May 2005, Cynosure granted approximately 18,000 options to non-employees under the 2004 Plan. In connection with this grant, Cynosure recorded $205,000 of stock-based compensation expense.

2005 Stock Incentive Plan

In August 2005, the Board of Directors adopted the 2005 Stock Incentive Plan (the 2005 Plan), which was approved by Cynosure's stockholders in December 2005. The 2005 Plan provided for the grant of ISOs, as well as nonstatutory options. The Board of Directors administers the 2005 Plan and had sole discretion to grant options to purchase shares of Cynosure's common stock.

The Board of Directors determines the term of each option, option price, number of shares for which each option is granted, whether restrictions would be imposed on the shares subject to options and the rate at which each option is exercisable. The exercise price for options granted is determined by the Board of Directors, except that for ISOs, the exercise price could not be less than the fair market value per share of the underlying common stock on the date granted (110% of fair market value for ISOs granted to holders of more than 10% of the voting stock of Cynosure). The term of the options is set forth in the applicable option agreement, except that in the case

of ISOs, the option term cannot exceed ten years. The number of shares of class A common stock reserved for issuance under the 2005 Plan is 1,288,369 shares. Options granted under the Plan vested either (i) over a 48-month period at the rate of 25% after the first year and 6.25% each quarter thereafter until fully vested or (ii) over a vesting period determined by the Board of Directors. As of December 31, 2007, there are 690,732 shares available for future grant under the 2005 Plan.

Stock option activity under the 1992 Plan, the 2004 Plan and the 2005 Plan is as follows:

	Number of Options	Exercise Price Range	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Life	Aggregate Intrinsic Value (in thousands)
Outstanding, December 31, 2006	2,154,662	$ 3.00 - $18.67	$ 6.46	8.18 years	$20,724
Granted	588,050	16.54 - 39.39	28.87		
Exercised	(1,237,831)	3.00 - 36.94	4.90		$29,922
Forfeited	(149,084)	3.00 - 36.94	8.95		
Outstanding, December 31, 2007	1,355,797	$ 3.00 - $39.39	$17.33	8.31 years	$14,863
Vested or expected to vest, December 31, 2007	1,301,892	$ 3.00 - $39.39	$17.29	8.31 years	$ 9,633
Exercisable, December 31, 2007	277,694	$ 3.00 - $36.94	$14.17	8.03 years	$ 3,592

14. Income Taxes

Income (loss) before income tax provision for (benefit from) income taxes and minority interest consists of the following:

	2007	2006	2005
		(In thousands)	
Domestic	$17,694	$(3,575)	$4,156
Foreign	5,094	2,705	176
Total	$22,788	$ (870)	$4,332

The provision for (benefit from) income taxes consists of:

	2007	2006	2005
		(In thousands)	
Current:			
Federal	$ 7,602	$ (125)	$ 1,573
State	471	43	119
Foreign	1,945	895	256
Total current	10,018	813	1,948
Deferred:			
Federal	(1,326)	(1,064)	(1,660)
State	(90)	(15)	(186)
Foreign	(326)	—	—
Total deferred	(1,742)	(1,079)	(1,846)
	$ 8,276	$ (266)	$ 102

A reconciliation of the federal statutory rate to Cynosure's effective tax rate is as follows for the years ended December 31:

	2007	2006	2005
Income tax provision (benefit) at federal statutory rate:	35.0%	(34.0)%	34.0%
Increase (decrease) in tax resulting from -			
State taxes, net of federal benefit	—	1.6	1.8
Nondeductible expenses	1.0	11.2	0.9
Tax-exempt interest income	(3.0)	(18.1)	—
Effect of foreign taxes	(1.8)	(22.1)	(38.5)
Stock-based compensation	0.3	22.2	3.7
Research and development credit	—	(5.5)	—
Write off of deferred assets	—	14.8	—
Effect of IRS exam settlement	4.2	—	—
Other	0.6	(0.7)	0.5
Effective income tax rate	36.3%	(30.6)%	2.4%

Significant components of Cynosure's net deferred tax assets as of December 31, 2007 and 2006 are as follows:

	2007	2006
	(In thousands)	
Deferred tax assets (liabilities):		
Domestic state net operating loss and tax credit carryforwards	$ 1	$ 224
Foreign net operating loss carryforwards	652	785
Reserves and allowances	2,141	1,605
Depreciation	207	200
Stock-based compensation	1,326	676
Other temporary differences	660	468
Gross deferred tax assets	4,987	3,958
Valuation allowance for deferred tax assets	(399)	(1,112)
Net deferred tax assets	$4,588	$ 2,846

As of December 31, 2007, Cynosure had foreign net operating loss carryforwards of approximately $2,367,000 available to reduce future foreign taxable income related to Germany. As of December 31, 2006, Cynosure maintained a full valuation allowance on all of its foreign deferred tax assets. During 2007, Cynosure made the determination that, based on the weight of all available evidence, it is now more likely than not that it will realize a tax benefit for its deferred tax assets in certain of its foreign jurisdictions. As a result, Cynosure has released the valuation allowance on the deferred tax assets in all of its foreign jurisdictions, with the exception of Germany. A tax benefit of $429,000 was realized in the foreign deferred tax provision for the release of this valuation allowance. The valuation allowance as of December 31, 2007 relates to state tax credit carryforwards and the German loss carryforwards.

In 2006, Cynosure adopted SFAS 123(R). In 2007, Cynosure recognized a total benefit of approximately $8,434,000 for stock-based compensation deductions, which was recorded through additional paid in capital. This amount represents the cash benefits that Cynosure will receive on its current year federal and state tax filings and through its current year federal loss carryback claim. Cynosure has approximately $3.8 million of additional net operating loss carryforwards and option deductions available to reduce state taxes payable in the future. Cynosure also has approximately $137,000 and $231,000 of federal and state credits, respectively, that, when utilized, will benefit additional paid in capital.

No amount for U.S. income tax has been provided on undistributed earnings of our foreign subsidiaries because the Company considers such earnings to be indefinitely reinvested. In the event of distribution of those earnings in the form of dividends or otherwise, Cynosure would be subject to both U.S. income taxes, subject to an adjustment, in any, for foreign tax credits, and foreign withholding taxes payable to certain foreign tax authorities. Determination of the amount of U.S. income tax liability that would be incurred is not practicable because of the complexities associated with this hypothetical calculation; however, unrecognized foreign tax credit carryforwards may be available to reduce some portion of the U.S. tax liability, if any.

Cynosure adopted the provisions of FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes, an Interpretation of FAS 109, Accounting for Income Taxes*, (FIN 48) on January 1, 2007. FIN 48 clarifies the accounting for income taxes, by prescribing a minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. FIN 48 also provides guidance on derecognition, measurement, classification, interest and penalties, accounting in interim periods, disclosure and transition.

Cynosure generally reports tax positions in its financial statements as they are reported on tax returns as filed or to be filed. A tax benefit is reflected in the financial statements only if it is "more-likely-than-not" that Cynosure will be able to sustain the tax position, based on its technical merits. Tax benefits from uncertain tax positions that reduce current or future income tax liabilities are reported in the financial statements only to the extent each benefit is recognized and measured, in accordance with the provisions of FIN 48. As a result of adopting FIN 48, Cynosure determined that no material cumulative effect adjustment was necessary to the opening balance of retained earnings as of January 1, 2007. Cynosure further determined, based on its analysis, that there were no significant unrecognized tax benefits that, if recognized, would affect the effective tax rate for the year ended December 31, 2007.

Under FIN 48, a tax return benefit that does not qualify for financial reporting recognition is generally treated as a government loan or incorrect application of a tax law and may result in interest and penalty charges. Cynosure classifies interest and penalties related to income taxes as a component of its provision for income taxes, and the amount of interest and penalties recorded during the year was immaterial.

Cynosure files income tax returns in the U.S. federal jurisdiction, and in various state and foreign jurisdictions. With few exceptions, Cynosure is no longer subject to U.S. federal, state and local, or non-U.S. income tax examinations by tax authorities for years before 2003.

As part of an Internal Revenue Service audit, Cynosure discovered in May 2007 that it erroneously claimed an intercompany bad-debt deduction from its German subsidiary of approximately $1.8 million on its 2003 U.S. federal income tax return. The deduction increased the amount of the U.S. net operating loss (NOL) carryforward as of December 31, 2003. During 2004 and 2005, the Company utilized this NOL carryforward to reduce taxable income and also recognized the financial statement benefit through a reduction in its tax provision for those two years. In accordance with SEC Staff Accounting Bulletin (SAB) No. 99 and SAB No. 108, Cynosure assessed the materiality of this error on its financial statements for the years ended December 31, 2004, 2005 and 2006 using both the roll-over method and iron-curtain method as defined in SAB No. 108. Cynosure concluded the effect of this error was not material to Cynosure's financial statements for the years ended December 31, 2004, 2005 and 2006 and, as such, these financial statements are not materially misstated. Cynosure also concluded that providing for the correction of the error in 2007 would not have a material effect on Cynosure's financial statements for the year ended December 31, 2007. As such, Cynosure recorded a provision for income taxes of $960,000 during the year ended December 31, 2007 for the tax liability and related interest required to correct this error. Cynosure settled the audit in 2008 and has included the expected liabilities in its accrued income taxes as of December 31, 2007.

15. 401(k) Plan

Cynosure sponsors the Cynosure 401(k) defined contribution plan. Participation in the plan is available to all employees of Cynosure who meet certain eligibility requirements. The Plan is qualified under Section 401(k) of the Internal Revenue Code, and is subject to contribution limitations as set annually by the Internal Revenue

Service. Employer matching contributions are at Cynosure's discretion. Cynosure's contributions to this plan totaled approximately $135,000 and $42,000 for the years ended December 31, 2007 and 2006, respectively. There were no employer matches for the year ended December 31, 2005.

16. Commitments and Contingencies

Lease Commitments

Cynosure leases its U.S. operating facility and certain foreign facilities under noncancelable operating lease agreements expiring through March 2012. Rent expense for the years ended December 31, 2007, 2006 and 2005 was approximately $1,276,000, $1,042,000 and $913,000, respectively.

Cynosure leases certain equipment and vehicles under operating and capital lease agreements with payments due through December 2012.

Commitments under Cynosure's lease arrangements are as follows, in thousands:

	Operating Leases	Capital Leases
2008	$1,203	$ 596
2009	1,078	458
2010	1,073	307
2011	1,086	133
2012	1,273	25
Total minimum lease payments	$5,713	$1,519
Less amount representing interest		(240)
Present value of obligations under capital leases		$1,279
Current portion of capital lease obligations		485
Capital lease obligations, net of current portion		$ 794

Lease Guarantees

During 2000 and 2001, Cynosure guaranteed the lease obligations for two locations that are operated by Sona MedSpa, and will be obligated to pay these leases if Sona MedSpa cannot make the required lease payments. Minimum lease payments guaranteed by Cynosure as of December 31, 2007 are as follows, in thousands:

2008	$ 54
2009	42
2010	42
2011	19
Total minimum lease payments guaranteed by Cynosure	$157

Litigation

In May 2005, Dr. Ari Weitzner, individually and as putative representative of a purported class, filed a complaint against Cynosure under the federal Telephone Consumer Protection Act, or TCPA, in Massachusetts Superior Court in Middlesex County seeking monetary damages, injunctive relief, costs and attorneys fees. The complaint alleges that Cynosure violated the TCPA by sending unsolicited advertisements by facsimile to the plaintiff and other recipients without the prior express invitation or permission of the recipients. Under the TCPA, recipients of unsolicited facsimile advertisements are entitled to damages of up to $500 per facsimile for inadvertent violations and up to $1,500 per facsimile for knowing or willful violations. Cynosure believes the

number of unsolicited facsimiles to be quite large. The plaintiff recently filed a motion seeking class certification, which Cynosure is opposing. Until this motion is ruled on, it would be premature to speculate about Cynosure's potential exposure in the case.

In December 2005, certain individuals commenced an arbitration against Cynosure along with Sona International Inc. Sona Med Spa Inc., Carousel Capital, Inc. and various individuals. The arbitration demand alleges fraud, violations of various state consumer protection laws and other causes of action in connection with the plaintiff's acquisition of franchises from the Sona entities. Cynosure declined to participate in the arbitration because Cynosure had not agreed contractually to do so, and it has been dismissed from the arbitration by agreement of the parties.

In January 2006, Gentle Laser Solutions, Inc., Liberty Bell Med Spa, Inc. and Kevin T. Campbell filed suit against Cynosure and one of its former directors, along with Sona International Inc. Sona Lasers Centers, Inc. and various other individuals, in the Superior Court of New Jersey. The matter was later removed to the United States District Court in the District of New Jersey. The suit alleges fraud, breach of contract and other causes of action in connection with the plaintiffs' acquisition of franchises from the Sona entities. The plaintiffs' and Sona have settled the plaintiffs' claims against Sona. Cynosure has moved to dismiss the plaintiffs' claims against the Company. Cynosure is not able to estimate the amount or range of loss that could result from an unfavorable outcome of the lawsuit as the matter is still in the early stages of the proceedings.

In June 2006, Baltimore Laser Solutions, Inc., and Kevin T. Campbell, filed suit against Cynosure and one of its former directors, along with Sona International Inc., Sona Lasers Centers, Inc. and various other individuals, in the United States District Court in the District of Maryland. The suit alleges fraud, breach of contract and other causes of action in connection with the plaintiffs' acquisition of franchises from the Sona entities. On April 11, 2007, upon a motion by the Sona defendants, the Court dismissed the suit in its entirety, without prejudice.

On January 9, 2008, Cynosure commenced a lawsuit in the U.S. District Court for the District of Massachusetts against CoolTouch Inc. for infringement of U.S. Patent No. 6,206,873, or the 873 patent. Cynosure's complaint alleges that CoolTouch's "CoolLipo" infringes on the 873 patent and seeks damages and injunctive relief. On January 31, 2008, CoolTouch answered Cynosure's complaint, denying liability and alleging that the 873 patent is not infringed and is invalid, and also asserted counterclaims against Cynsorure in the same court alleging patent infringement by Cynosure. CoolTouch's counterclaim alleges that Cynosure's *Affirm* product infringes U.S. Patent Nos. 7,122,029 and 6,451,007, and that its *Smartlipo* product infringes U.S. Patent No. 7,217,265, and seeks damages in an unspecified amount, as well as injunctive relief. Cynosure is vigorously prosecuting its claims against CoolTouch and defending against CoolTouch's counterclaims. Cynosure is not able to estimate the amount or range of loss that could result from an unfavorable outcome of the lawsuit as the matter is still in the early stages of the proceedings.

In addition to the matters discussed above, from time to time, Cynosure is subject to various claims, lawsuits, disputes with third parties, investigations and pending actions involving various allegations against Cynosure incident to the operation of its business, principally product liability. Each of these other matters is subject to various uncertainties, and it is possible that some of these other matters may be resolved unfavorably to Cynosure. Cynosure establishes accruals for losses that management deems to be probable and subject to reasonable estimate. Cynosure believes that the ultimate outcome of these matters will not have a material adverse impact on its consolidated financial position, results of operations or cash flows.

17. Summary Selected Quarterly Financial Data (Unaudited)

The following table sets forth certain unaudited consolidated quarterly statement of operations data for the twelve quarters ended December 31, 2007. This information is unaudited, but in the opinion of management, it has been prepared substantially on the same basis as the audited consolidated financial statements and all necessary adjustments, consisting only of normal recurring adjustments, have been included in the amounts stated below to state fairly the unaudited consolidated quarterly results of operations. The results of operations for any quarter are not necessarily indicative of the results of operations for any future period.

	Quarter Ended			
	March 31, 2007	June 30, 2007	Sept. 30, 2007	Dec. 31, 2007
	(In thousands, except per share data)			
Revenues	$26,077	$30,132	$31,533	$36,573
Gross profit	$16,155	$19,064	$20,488	$24,101
Income from operations	$ 2,875	$ 4,489	$ 5,567	$ 6,646
Net income	$ 2,118	$ 2,711	$ 4,377	$ 5,306
Basic net income per share	$ 0.19	$ 0.23	$ 0.36	$ 0.43
Diluted net income per share	$ 0.17	$ 0.21	$ 0.34	$ 0.41

	Quarter Ended			
	March 31, 2006	June 30, 2006	Sept. 30, 2006	Dec. 31, 2006
	(In thousands, except per share data)			
Revenues	$17,139	$18,131	$18,556	$24,575
Gross profit	$ 9,107	$10,590	$11,114	$14,670
Income (loss) from operations	$ 294	$ 1,371	$(8,506)	$ 2,461
Net income (loss)	$ 626	$ 1,441	$(4,247)	$ 1,530
Basic net income (loss) per share	$ 0.06	$ 0.13	$ (0.38)	$ 0.14
Diluted net income (loss) per share	$ 0.05	$ 0.12	$ (0.38)	$ 0.13

EXHIBIT INDEX

Exhibit Number	Description
3.1	Restated Certificate of Incorporation of the Registrant (Incorporated by reference to the exhibits to the Registrant's Registration Statement on Form S-1 (333-127463))
3.4	Amended and Restated Bylaws of the Registrant (Incorporated by reference to the exhibits to the Registrant's Registration Statement on Form S-1 (333-127463))
4.1	Specimen certificate evidencing shares of class A common stock (Incorporated by reference to the exhibits to the Registrant's Registration Statement on Form S-1 (333-127463))
10.1*	1992 Stock Option Plan (Incorporated by reference to the exhibits to the Registrant's Registration Statement on Form S-1 (333-127463))
10.2*	2004 Stock Option Plan, as amended (Incorporated by reference to the exhibits to the Registrant's Registration Statement on Form S-1 (333-127463))
10.3*	2005 Stock Incentive Plan (Incorporated by reference to the exhibits to the Registrant's Registration Statement on Form S-1 (333-127463))
10.4*	Employment Agreement, dated September 2003, between the Registrant and Michael Davin (Incorporated by reference to the exhibits to the Registrant's Registration Statement on Form S-1 (333-127463))
10.5*	Employment Agreement, dated January 1, 2003, between the Registrant and George Cho (Incorporated by reference to the exhibits to the Registrant's Registration Statement on Form S-1 (333-127463))
10.6*	Employment Agreement, dated September 2003, between the Registrant and Douglas Delaney (Incorporated by reference to the exhibits to the Registrant's Registration Statement on Form S-1 (333-127463))
10.7†	Distribution Agreement, effective as of January 1, 2005, between the Registrant and El.En. S.p.A. (Incorporated by reference to the exhibits to the Registrant's Registration Statement on Form S-1 (333-127463))
10.8†	Distribution Agreement, effective as of January 1, 2005, between the Registrant and El.En. S.p.A. (Incorporated by reference to the exhibits to the Registrant's Registration Statement on Form S-1 (333-127463))
10.9	Promissory Note, dated October 1, 2004, between the Registrant and El.En. S.p.A. (Incorporated by reference to the exhibits to the Registrant's Registration Statement on Form S-1 (333-127463))
10.10	Lease, dated January 31, 2005, between Glenborough Fund V, Limited Partnership and the Registrant, as amended
10.11	Reimbursement Agreement among the Registrant, El.En. S.p.A. and BRCT, Inc. (Incorporated by reference to the exhibits to the Registrant's Registration Statement on Form S-1 (333-127463))
10.12*	Option Agreement, dated December 17, 2003, between El.En. and Michael Davin (Incorporated by reference to the exhibits to the Registrant's Registration Statement on Form S-1 (333-127463))
10.13*	Option Agreement, dated May 13, 2005, between El.En. and Michael Davin (Incorporated by reference to the exhibits to the Registrant's Registration Statement on Form S-1 (333-127463))
10.14	Non-Exclusive Patent License, dated November 6, 2006, between Palomar Medical Technologies, Inc. and the Registrant (Incorporated by reference to the exhibit to the Registrant's current report on Form 8-K filed November 7, 2006)

Exhibit Number	Description
21.1	Subsidiaries of the Registrant
23.1	Consent of Ernst & Young LLP
31.1	Certification of the Principal Executive Officer
31.2	Certification of the Principal Financial Officer
32.1	Certification of the Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Certification of the Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

* Management contract or compensation plan or arrangement required to be filed as an exhibit pursuant to Item 15(c) of Form 10-K.

† Confidential treatment granted as to certain portions, which portions have been omitted and filed separately with the Securities and Exchange Commission.

Exhibit 31.1

CERTIFICATIONS

I, Michael R. Davin, certify that:

1. I have reviewed this Annual Report on Form 10-K of Cynosure, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this annual report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statement for external purposes in accordance with generally accepted accounting principles;

c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ MICHAEL R. DAVIN

Michael R. Davin
Chairman, President and Chief Executive Officer

Date: March 13, 2008

Exhibit 31.2

CERTIFICATIONS

I, Timothy W. Baker, certify that:

1. I have reviewed this Annual Report on Form 10-K of Cynosure, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this annual report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statement for external purposes in accordance with generally accepted accounting principles;

c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ TIMOTHY W. BAKER

Timothy W. Baker
Executive Vice President,
Chief Financial Officer and Treasurer

Date: March 13, 2008

Exhibit 32.1

**CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Annual Report on Form 10-K of Cynosure, Inc. (the "Company") for the period ended December 31, 2007 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned, Michael R. Davin, Chairman, President and Chief Executive Officer of the Company, hereby certifies, pursuant to 18 U.S.C. Section 1350, that to his knowledge:

(1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ MICHAEL R. DAVIN

Michael R. Davin
Chairman, President and Chief Executive Officer

Date: March 13, 2008

Exhibit 32.2

**CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Annual Report on Form 10-K of Cynosure, Inc. (the "Company") for the period ended December 31, 2007 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned, Timothy W. Baker, Executive Vice President, Chief Financial Officer and Treasurer of the Company, hereby certifies, pursuant to 18 U.S.C. Section 1350, that to his knowledge:

(1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

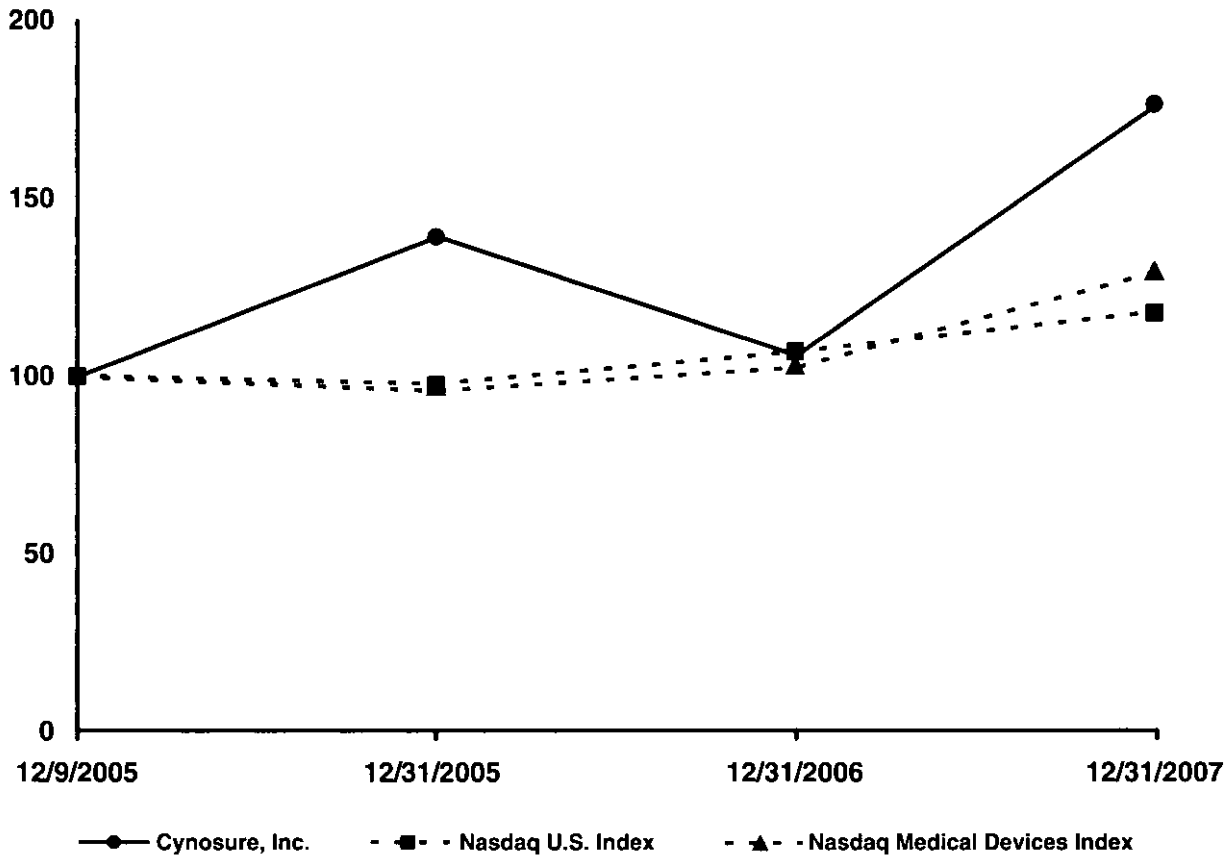
/s/ TIMOTHY W. BAKER

Timothy W. Baker
Executive Vice President,
Chief Financial Officer and Treasurer

Date: March 13, 2008

COMPARATIVE STOCK PERFORMANCE

The following graph compares cumulative total shareholder return on our class A common stock from December 9, 2005, the date our class A common stock commenced trading on the Nasdaq National Market, through December 31, 2007 with the cumulative total return for the Nasdaq U.S. Index and the Nasdaq Medical Devices Index. This graph assumes investment of $100 on December 9, 2005 in our common stock, the Nasdaq U.S. Index and the Nasdaq Medical Devices Index and assumes all dividends are reinvested. We have never paid dividends on our class A common stock and have no present plans to do so.



Company/Index	12/09/2005	12/31/2005	12/31/2006	12/31/2007
Cynosure, Inc.	$100	$139.07	$105.54	$176.41
NASDAQ U.S. Index	$100	$ 97.65	$107.20	$117.83
NASDAQ Medical Devices Index	$100	$ 96.78	$102.07	$128.84

Cynosure, Inc. Corporate and Stockholder Information

Board of Directors

Ettore V. Biagioni[1,3]
Managing Partner, Alothon Group LLC

Andrea Cangioli
Director and General Manager, El.En.

Michael R. Davin
President and Chief Executive Officer, Cynosure, Inc.
Chairman of the Board

Paul F. Kelleher[2,3]
Corporate Advisor
Chairman, Audit Committee

Leonardo Masotti
Professor of Electronics, University of Florence, Italy

Thomas H. Robinson
Managing Partner of Medical Technology Practice,
Spencer Stuart, Inc.
Chairman, Compensation Committee

George J. Vojta[1,2]
President and Director, Financial Services Forum
Chairman, Corporate Governance Committee

1 Audit Committee member
2 Compensation Committee member
3 Corporate Governance Committee member

Management

Michael R. Davin
President, Chief Executive Officer and Chairman

Timothy W. Baker
Executive Vice President, Chief Financial Officer
and Treasurer

Douglas J. Delaney
Executive Vice President, Sales

Rafael Sierra
Chief Technology Officer

George Cho
Senior Vice President, Medical Technology and
Regulatory Affairs

Kenji Shimizu
Senior Vice President, International Sales

Marina Kamenakis
Vice President, Clinical Development

David Mackie
Executive Vice President, Operations

James Palastra
Vice President, Customer Service

James Boll
Vice President, Engineering

Corporate Information

Transfer Agent and Registrar
American Stock Transfer & Trust Company
59 Maiden Lane
New York, NY 10038
800-937-5449

2008 Annual Meeting of Stockholders
Wednesday, May 14, 2008, 10:00 a.m.
Wilmer Cutler Pickering Hale and Dorr LLP
60 State Street
Boston, Massachusetts 02109

Corporate Counsel
Wilmer Cutler Pickering Hale and Dorr LLP
60 State Street
Boston, Massachusetts 02109
617-526-6000

Independent Registered Public Accounting Firm
Ernst & Young LLP
200 Clarendon Street
Boston, Massachusetts 02216
617-266-2000

Stock Trading Information
The Nasdaq Global Market
Symbol: CYNO

Investor Contact
Financial results, corporate news, SEC filings and
company information is available on Cynosure's
website at www.cynosure.com.

For additional information, please contact:

Cynosure, Inc.
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Email: investor@cynosure.com

CYNOSURE
Be transformed™

www.cynosure.com

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END